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IN THE

Supreme Court of the United States

BAXTER INTERNATIONAL, INCORPORATED,
Petitioner,

v.

ABBOTT LABORATORIES,
Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether an arbitration panel may shield its award from court review for compliance with public policy because the panel itself concluded that the award does no violence to a specific public policy favoring competition embodied in the antitrust laws?

CORPORATE DISCLOSURE STATEMENT

Petitioner Baxter International, Incorporated has no parent company and no publicly held corporation owns 10% or more of Petitioner's stock.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner Baxter International, Incorporated respectfully requests that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit in this case.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Seventh Circuit was entered on January 16, 2003 and is included in the Appendix ("App.") at 1a-18a. It has been officially reported and can be found at *Baxter International, Inc.* v. *Abbott Laboratories*, 315 F.3d 829 (7th Cir. 2003). Baxter's petition for rehearing en banc was denied on April 10, 2003. The order denying the petition and the dissenting opinion accompanying that order are included in the Appendix at 92a-94a. They, too, were officially reported and can be found at *Baxter International, Inc.* v. *Abbott*

Laboratories, 325 F.3d 954 (7th Cir. 2003). The March 27, 2002 opinion of the district court is not reported, but is reproduced in the Appendix at 19a-42a.

JURISDICTION

The court of appeals entered its opinion and judgment on January 16, 2003. Petitioner timely filed its petition for rehearing en banc on January 30, 2003. That petition was denied on April 10, 2003. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

TREATY PROVISION INVOLVED

The arbitral award in this case falls within the scope of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, *done* June 10, 1958 (entered into force for the United States Dec. 29, 1970) ("New York Convention"), which is reproduced in the notes to 9 U.S.C. § 201. Article V, § 2(b) of the New York Convention provides:

> Recognition and enforcement of an arbitral award may ... be refused if the competent authority in the country where recognition and enforcement is sought finds that ... [t]he recognition or enforcement of the award would be contrary to the public policy of that country.

STATEMENT OF THE CASE

This Court has long recognized that public policy is a significant constraint on the enforceability of arbitration awards. See *W.R. Grace & Co.* v. *Local Union 759*, 461 U.S. 757 (1983). Courts asked to approve such awards have routinely declined to do so when the ultimate effect of the arbitration decision conflicts with federal law (here, the antitrust laws) and thus does violence to public policy norms. To be sure, courts are not free to use public policy as an

excuse for setting aside awards with which they disagree; that would invade the province of the arbitral process. By the same token, until the decision in this case, arbitrators were not authorized effectively to preempt judicial scrutiny of the consistency between their awards and public policy as embodied in federal law by purporting to decide that issue as part of the arbitration. The Seventh Circuit abdicated its responsibility to ensure that public policy is not vitiated by private arbitrators. This fundamental departure from the rulings of this Court and the courts of appeals warrants certiorari.

A. The Sevoflurane Agreements.

This case concerns Petitioner's effort to market a generic version of a successful inhalable anesthetic, sevoflurane, in competition with Abbott Laboratories' ("Abbott's") brand-name product. Petitioner invented sevoflurane in the mid-1960s, but no commercially viable process for producing it existed until the early 1980s when Petitioner obtained patents on the "one-step process" for making sevoflurane. App. 1a. Petitioner then licensed its patents on both the sevoflurane molecule and the one-step process to a Japanese company, Maruishi, so that Maruishi could obtain regulatory approval to market sevoflurane in Japan and other Asian countries. In the early 1990s, Maruishi, having obtained regulatory approval, introduced sevoflurane in Japan, where the product was a commercial success.

Petitioner and Maruishi then turned their attention to the United States. Maruishi decided not to introduce sevoflurane in the United States itself, opting instead to sublicense its rights to Respondent Abbott Laboratories. In 1992, after lengthy and detailed negotiations, Petitioner entered into a new licensing agreement with Maruishi, which gave Maruishi the right to grant sublicenses, and Maruishi entered into a separate sublicensing agreement with Abbott.

Because Petitioner's patents on sevoflurane itself and the method of using it as an anesthetic had expired in 1989, that product and method were already in the public domain by 1992. *Dastar Corp.* v. *Twentieth Century Fox Film Corp.*, 123 S. Ct. 2041, 2048 (2003) ("'the right to make [an article whose patent has expired] – including the right to make it in precisely the shape it carried when patented – passes to the public'") (alteration in original) (quoting *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, 230 (1964)). As a result, the 1992 license and sublicense could not and did not convey rights to sevoflurane itself or to its use as an anesthetic. Instead, the license and sublicense conveyed rights only to the one-step process patents and related know-how. The parties thus were fully aware that Abbott could face competition for the sale of sevoflurane in the United States, even before the licensed patents expired in 2005, from generic producers who developed processes for producing sevoflurane that did not infringe the one-step process patents. Indeed, Abbott expressly anticipated and planned for such competition to arrive by 2000.

Although Petitioner and Abbott did not enter into any license agreements with each other, both Petitioner and Abbott along with Maruishi (and a fourth party not relevant to these proceedings) entered into a separate Dispute Resolution Agreement. That agreement provided that, if a dispute arose under the sevoflurane agreements, the parties agreed first to negotiate, then to mediate, and finally, if necessary, to arbitrate. App. 105a-107a. In the event arbitration became necessary, the agreement expressly set a standard to guide the conduct of the arbitrators. They should strive to prevent an "Impairment of the Original Commercial Relationship." *Id.* at 97a. This "Impairment of the Original Commercial Relationship" was defined to include "an alleged breach or termination of one of the Sevoflurane Agreements that results or could reasonably be expected to result in any change or potential change in the Original Commercial Relationship that

would ... reduce the amount a party would but for such change otherwise receive under any Sevoflurane Agreement." *Id.* at 97a-98a. In discharging that duty, the arbitrators were directed to employ "sound and impartial business judgment," which is also what the agreement directed executives of the parties to employ during pre-arbitration negotiations concerning any disputes. *Id.* at 97a.

B. Abbott Introduces Sevoflurane In The United States And Ohmeda, As Expected, Develops A Generic Competitor.

After obtaining the necessary FDA approval, Abbott began marketing sevoflurane in the United States in 1995. App. 2a. Abbott has enjoyed market exclusivity in the United States ever since, even though it anticipated that generic competition would likely arise by 2000, well before the expiration of the process patents that were licensed to it.

As Abbott had anticipated, a competitor, Ohmeda, by 1997 had developed a commercially viable process for making sevoflurane (the "three-step process") that did not infringe the licensed one-step process. Ohmeda built a pilot plant and prepared plans for a full-scale production facility so that it could, after it obtained FDA approval, compete with Abbott. In April 1998, after Ohmeda had developed the three-step process and its plans to compete, Petitioner acquired Ohmeda.

C. The Parties Enter Arbitration To Determine The Scope Of The Sevoflurane Agreements.

In September 1998, Petitioner informed Maruishi of its intention to pursue Ohmeda's plans to develop and market a non-infringing generic sevoflurane in the United States. When Abbott learned of Petitioner's plan, it invoked the procedures of the Dispute Resolution Agreement. After efforts to negotiate and mediate a resolution failed, Abbott submitted its claim for arbitration.

Abbott asked the arbitrators for an order preventing Petitioner from selling generic sevoflurane until the sevoflurane agreements expire in 2005. Abbott thus asked the arbitrators to impose a covenant not to compete between Petitioner and Abbott with respect to a product that is in the public domain. Such a covenant not to compete would be a *per se* violation of Section 1 of the Sherman Act if it resulted from a direct agreement between the parties. See, *e.g.*, *In re Cardizem CD Antitrust Litig.*, No. 00-2483, 2003 WL 21360049, at *2, *7-*8 (6th Cir. June 13, 2003) (holding that agreement by which brand name manufacturer pays generic seller to keep its FDA-approved generic product off the market is a *per se* violation of the antitrust laws).

During the arbitration, Abbott asserted a variety of bases for the order it sought which, had they been well founded, might have rendered it consistent with the Sherman Act. Abbott claimed that the three-step process would, in fact, infringe the licensed one-step process patents. The arbitrators disagreed. App. 59a. Abbott also claimed that the three-step process was an improvement on the one-step process or that Petitioner had developed the three-step process using know-how derived from the one-step process, thus breaching the exclusive license that Petitioner had granted to Maruishi. The arbitrators also rejected these claims. *Id.*

In sum, the arbitrators expressly concluded that the licensing agreement did not contain the covenant not to compete that Abbott sought. App. 63a-64a. Instead, two of the three arbitrators, over the dissent of the third, determined that they were authorized to impose a covenant not to compete based on the broad authority they were given in the Dispute Resolution Agreement. The majority reasoned, as Abbott had argued, that if Petitioner sold generic sevoflurane, then Abbott would receive less money from sales of its own sevoflurane. Of course, this is only because of the monopoly rents that Abbott could extract by eliminating Petitioner as a competitor. The majority reasoned that the Dispute

Resolution Agreement empowered the arbitrators, even absent a breach of the Baxter-Maruishi licensing agreement,[1] to prevent an "Impairment of the Original Commercial Relationship" by preventing Petitioner from taking any action that would "'reduce the amount [Abbott] would ... otherwise receive'" from its sales of sevoflurane. *Id.* at 61a (emphasis omitted). They thus barred Petitioner from introducing its generic drug in competition with Abbott. *Id.* at 67a.

As is plain, nothing in the *claims* Abbott presented to the arbitrators involved antitrust law. Rather, Petitioner perceived that the order Abbott sought could be deemed an agreement between Petitioner and Abbott (the arbitrators being the mere agents of the parties) to allocate markets in violation of Section 1 of the Sherman Act. Petitioner argued that the order Abbott sought would, therefore, violate the public policy, reflected in the Sherman Act, prohibiting a naked horizontal market allocation. Petitioner also pointed out that the result that Abbott sought would violate the public policy reflected in a Consent Decree that Abbott had entered into with the Federal Trade Commission.[2] As Petitioner explained, the sevoflurane agreements "cannot be interpreted

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[1] The Seventh Circuit panel majority thus erred when it stated that the arbitrators ruled that Baxter's sale of generic sevoflurane would violate the Baxter-Maruishi license. App. 3a. The arbitrators specifically concluded to the contrary, *id.* at 63a-64a, and believed that they were authorized to impose a covenant not to compete even in the absence of a breach of the license agreement. *Id.* at 61a.

[2] In May 2000, Abbott and the FTC entered into a consent decree arising from an agreement between Abbott and Geneva Pharmaceuticals in which Abbott had agreed to pay Geneva $4.5 million per month to delay the introduction of Geneva's generic version of terazosin hydrochloride, a drug for which Abbott was the exclusive, brand-name seller. Pursuant to the terms of the Consent Decree, Abbott must refrain from "being a party" to agreements with generic drugmakers that would keep generic products off the market beyond the point in time at which the FDA would permit them to enter that market. By virtue of the arbitrators' ruling, Abbott is now a party to such an agreement with Petitioner.

in a way [that] violates public policy." Arbitration Hr'g Tr. at 1478, *Abbott Labs.* v. *Baxter Int'l* (CPR Inst. heard Mar. 8, 2001). In one brief paragraph, the arbitrators summarily decided that "no illegality results from" the non-compete covenant they were creating. App. 66a-67a.

D. Federal Court Review Of The Arbitral Award.

Abbott petitioned the United States District Court for the Northern District of Illinois to enforce the arbitral award pursuant to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("New York Convention"). In its response, Petitioner recognized that the fundamental issue of contract interpretation, *i.e.*, whether the Dispute Resolution Agreement empowered the arbitrators to impose a covenant not to compete, could not be reargued. However, because a federal court was being asked, pursuant to the New York Convention, to enforce the arbitral award, the district court necessarily had to decide whether it should refuse to enforce the award because the award is "contrary to the public policy of" the United States. New York Convention, art. V, § 2(b), *reproduced in* 9 U.S.C. § 201 note. Petitioner argued that the award violated the public policy of the United States as reflected in both Section 1 of the Sherman Act and the Abbott/FTC Consent Decree.

The district court did not hesitate to review the public policy question. App. 31a. After conducting its own analysis of the issues, the court concluded – wrongly – that Petitioner had failed to establish either an antitrust violation or a violation of the Abbott/FTC Consent Decree. *Id.* at 31a-39a (antitrust), 39a-40a (Consent Decree).

The Seventh Circuit, by a two-to-one vote, affirmed. Unlike the district court, however, the panel majority flatly refused to consider the merits of Petitioner's challenge to the award as a horizontal market allocation that violated Section 1 of the Sherman Act and the Abbott/FTC consent decree. The panel determined that it had no authority even to reach

Petitioner's public policy argument because the arbitrators had considered and reached their own conclusion on that issue. As the panel viewed the matter, once the arbitrators rejected Petitioner's argument that Abbott's interpretation of the contract would compel unlawful conduct (both under the antitrust laws and the consent decree), a federal court had no choice but to confirm the award. Petitioner could not ask a federal court to refuse to confirm the award, even if confirming the award would effectively order the parties to eliminate competition in a market for an important medical product. App. 4a.

The panel majority acknowledged Petitioner's argument that the arbitrators had *created* and not merely decided an antitrust issue. App. 5a. That is, Petitioner's public policy challenge focused exclusively on the *effect* of the arbitrators' award, and did not challenge the arbitrators' view that the Dispute Resolution Agreement authorized them to impose a covenant not to compete. As the panel majority recognized, Petitioner invoked the rule that prohibits an arbitrator to "command the parties to violate rules of positive law." *Id.* But, to the panel majority, "*whether* the tribunal's construction of the ... agreement has [the effect of commanding the parties to violate the law] was a question put to, and resolved by, the arbitrators. They answered no, and as between Baxter and Abbott their answer is conclusive." *Id.* at 5a-6a. On this basis, the panel majority decided that a federal court could not independently review whether the arbitrators were commanding the parties to violate the law.

Judge Cudahy dissented. Judge Cudahy reasoned that Petitioner's decision to urge the arbitrators not to read the contract to impose an unlawful covenant not to compete did not divest a federal court of authority independently to review the award to determine whether it did command the parties to violate the antitrust laws. Judge Cudahy perceived "an important distinction" between "a simple [antitrust] claim by Baxter against Abbott," on the one hand, and "a request by

Baxter that the arbitrators step back and consider the larger implications of their underlying decision," on the other. App. 12a n.3. Judge Cudahy recognized that a court would surely defer to the arbitrators' ruling in the former situation. *Id.* at 11a-12a.

But this case presented the latter. When the arbitrators examined Petitioner's contention that Abbott's proposed order would be an unlawful covenant not to compete, they were "reviewing their own decision" in precisely the way a court would. App. 13a n.5. Specifically, the arbitrators were examining their interpretation of the Dispute Resolution Agreement to determine whether any "'illegality results'" from the award. *Id.* (citing App. 66a). Judge Cudahy argued that to allow an arbitration panel to insulate its decision from court review through the simple expedient of declaring that its decision does not command the parties to violate the law creates an exception that swallows the rule: "[U]nder the majority's analysis, the rule that unlawful conduct cannot be commanded by arbitrators is consumed by the exception that, if the arbitrators themselves say that what they have commanded is not unlawful, then 'their answer is conclusive.'" *Id.* at 13a.

Judge Cudahy then analyzed the merits of Petitioner's antitrust challenge. Judge Cudahy recognized that an agreement among competitors that, in isolation, reduces competition may be a necessary part of a cooperative venture (like the agreements that brought sevoflurane to the United States) that, on the whole, benefits consumers. App. 15a. But the covenant not to compete imposed by the arbitrators here was not of that sort. It was in no way a necessary part of the agreements that brought sevoflurane to the United States. Competition from Petitioner was not a major concern in 1992, especially after Petitioner had licensed away not only the one-step process, but also any improvements thereon and all of its related know-how. Abbott knew that competition from companies like Ohmeda was on the horizon, and a broad

covenant not to compete from Petitioner would have provided no protection against that. In short, Judge Cudahy could find no reason to believe that Abbott considered a broad covenant not to compete from Petitioner an essential part of the arrangement, especially in light of the fact that Abbott had failed to include any language to that effect in the parties' lengthy and detailed agreements. Thus, Judge Cudahy concluded that the arbitrators' award effects an unlawful horizontal allocation of markets that is not ancillary to any procompetitive agreement. *Id.* at 15a-17a.

Petitioner sought en banc review. By a vote of five to three, the court denied the petition.[3] Judge Ripple issued an opinion dissenting from the denial of rehearing *en banc*, joined by Judges Diane P. Wood and Williams. The dissenters recognized that "the scope of judicial review of arbitral decisions that, at least arguably, order the parties to violate the law is an important issue." App. 93a. Further, the dissent indicated that the panel majority's holding is "difficult to square with existing Supreme Court precedent and, indeed, with the precedent of this circuit and our sister circuits." *Id.*

REASONS FOR GRANTING THE PETITION

The Seventh Circuit's ruling has broken new and unsettling ground regarding the important and recurring issue of court review of arbitral awards. The panel majority's view, that arbitrators have the power to shield their own orders from court review for compliance with the dictates of federal law in general and the Sherman Act in particular, cannot be squared with this Court's precedent, with the precedent of the other federal courts of appeals, with the New York Convention, or with sound arbitration policy. The panel's decision threatens

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[3] Three judges recused themselves from considering the petition. The order denying rehearing en banc lists nine judges, but Judge Cudahy, who served on the panel, is a senior judge and therefore did not participate in the "vote of the active members of the court." App. 92a.

both to discourage arbitration as a means of resolving disputes, thus increasing the burdens on the federal courts, and to undermine the uniform rules defining the boundaries between courts and arbitrators. The Court should grant this petition to preserve the effect of its own prior decisions, to promote the federal policy favoring arbitration, and to ensure a uniform national approach to court review of arbitral awards for compliance with public policy.

1. The Decision Below Is Contrary To This Court's Decisions. Arbitrators have broad discretion to interpret the parties' contract. Parties generally may not ask courts to correct arbitrators' errors of contract interpretation. *United Steelworkers of Am.* v. *Enterprise Wheel & Car Corp.*, 363 U.S. 593, 596-99 (1960). Accordingly, if the arbitrators interpret a contract in a way that requires a party to violate the law or is otherwise inconsistent with public policy, that party may not ask a court to read the contract differently; issues of contract interpretation are exclusively the province of the arbitrators.

But that proposition does not remotely suggest that a party may not ask a court to refuse to enforce the award because it violates public policy. In a series of cases beginning with *W.R. Grace & Co.* v. *Local Union 759*, 461 U.S. 757 (1983), and continuing through *Mitsubishi Motors Corp.* v. *Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985), and *Vimar Seguros Y Reaseguros, S.A.* v. *M/V Sky Reefer*, 515 U.S. 528 (1995), this Court has addressed that question and recognized that protecting the dictates of public policy is solely the province of the judiciary. In this series of cases, the Court has indicated that arbitrators have the authority to consider, in the first instance, whether one party's interpretation of a contract would violate public policy. But even as these cases permit arbitrators to consider the public policy implications of proposed contractual interpretations, they make clear that, regardless of whether the arbitrator considers the public policy issue, the ultimate authority to ensure that an arbitral

order does no injury to the commands of specific public policies rests with the courts.

W.R. Grace involved a dispute between certain union members and their employer. The employer, Grace, had laid off the union members pursuant to an agreement Grace had with the EEOC regarding past discrimination and its seniority system's effect of perpetuating that discrimination. The agreement with the EEOC was inconsistent with Grace's collective bargaining agreement with its union. 461 U.S. at 760. Grace obtained a district court judgment stating that the terms of the EEOC agreement were binding on all parties, including Grace and the union, regardless of any inconsistency with the collective bargaining agreement. *Id.* at 761. Later the Fifth Circuit reversed and Grace reinstated the laid-off workers.

Pursuant to the collective bargaining agreement, the employees initiated arbitration to collect back pay for the time they were out of work. *Id.* at 762. Grace argued that the district court's order enforcing the agreement with the EEOC precluded an award of back pay, because Grace was complying with that court order during the period for which the employees were seeking back pay. The arbitrator concluded that the collective bargaining agreement did not preclude an award of back pay even if the employees were laid off in compliance with a then-valid court order. *Id.* at 763-64.

This Court refused to reconsider the arbitrator's interpretation of the collective bargaining agreement. *Id.* at 765-66. Thus, this Court accepted that the arbitrator had properly interpreted the contract to require Grace to compensate the employees with back pay, even though Grace was complying with a court order during the relevant period.

Still, this Court reviewed the arbitrator's award for compliance with public policy. It did so because "a court *may not enforce* a collective-bargaining agreement that is contrary

to public policy." *Id.* at 766 (emphasis added). Even though the Court accepted that the arbitrator's reading of the collective bargaining agreement was correct, the Court still independently reviewed the agreement, as interpreted by the arbitrator, to ensure compliance with public policy before enforcing the arbitrator's ruling. Although the arbitrator in *Grace* had not himself considered the public policy question, this Court specifically indicated that it would not have mattered if he had. The arbitrator's "view of his own jurisdiction precluded his consideration of th[e public policy] question, *and, in any event*, the question of public policy is ultimately one for resolution by the courts." *Id.* (emphasis added); see *United Paperworkers Int'l Union* v. *Misco, Inc.*, 484 U.S. 29, 43 (1987) (stating that a decision regarding whether an award violates public policy "turn[s] on *our* examination of whether the award created any explicit conflict with other 'laws and legal precedents'") (emphasis added). Ultimately, this Court found that the arbitrator's ruling was not contrary to public policy and enforced it. But it did so only after reviewing *de novo* the public policy question on its merits. *W.R. Grace*, 461 U.S. at 766-72.

Mitsubishi confirms the approach outlined in *W.R. Grace*. The principal issue in *Mitsubishi* was whether antitrust claims could be submitted to a foreign arbitration panel, and this Court answered that they could. But the United States, as *amicus*, expressed concern that the arbitrators might read the choice-of-law clause (Swiss law) in combination with the forum-selection clause (Japanese arbitration) "wholly to displace American law." 473 U.S. at 637 n.19. The effect of such an interpretation would be that the clauses "operated in tandem as a prospective waiver of a party's right to pursue statutory remedies for antitrust violations." *Id.* Because the arbitration panel had not yet interpreted the contract that way, this Court had no "occasion to speculate on this matter at this stage in the proceedings." *Id.* Nevertheless, this Court made clear that at a later stage in the proceedings, if the arbitrators

in fact read the contract as the United States feared, "we would have little hesitation in condemning the agreement as against public policy." *Id.* The Court cited a variety of cases that stand for the settled rule prohibiting parties by private agreement from releasing each other from antitrust liability arising out of their own agreements. *Id.* Put simply, if the arbitrators, over one party's public policy objection, decided to read the contract as an unlawful prospective waiver of remedies under the Sherman Act, that ruling would not be enforceable by a court.

In *Vimar*, the Court, for a third time, took the same approach to federal review of arbitral awards for violations of public policy. *Vimar* involved a dispute between the owner of a shipload of fruit that had been damaged in transit and the owner of the vessel transporting the fruit. The agreement between the parties required arbitration in Japan. The transaction between the parties was subject to the federal Carriage of Goods by Sea Act ("COGSA"). The fruit owner argued that the Court should not send the case to arbitration because certain Japanese rules, potentially applicable because of the agreement's choice-of-law provision, were inconsistent with COGSA regarding whether the shipowner could defend against the claim based on acts or omissions by the stevedores hired by the shipowner. 515 U.S. at 539.

This Court, acknowledging that the concern was substantial, refused to decide how such a conflict between COGSA and the Japanese rules, if any conflict existed, should be resolved. Instead, this Court held that the arbitrators should consider the question in the first instance. This disposition was justified because court review remained available if the arbitrators ruled both that the Japanese rules applied under the contract and interpreted those rules in a manner inconsistent with COGSA. *Id.* at 540. Relying on *Mitsubishi*, this Court said that the district court would, at the award enforcement stage, have a duty to ensure that that the

construction of the contract and the award are not inconsistent with the public policy reflected in COGSA. *Id.*

In sum, this Court has rejected the outdated suspicion that courts once held for arbitrators. "[W]e are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as an alternative means of dispute resolution." *Mitsubishi*, 473 U.S. at 626-27. But the federal policy in favor of arbitration has not led this Court as far as the decision below takes the law: courts abdicating to arbitrators the authority to review awards to ensure that they do not command the parties to violate the law and hence violate public policy. The issue whether the arbitral award so departs from public policy as to be unenforceable remains, under this Court's opinions, the province ultimately of the courts.

All of this produces a simple and sensible approach for dealing with a contract that could potentially be interpreted to violate public policy. The arbitrator should, in the first instance, consider the public policy challenge to a party's proposed contractual interpretation. And, if the arbitrator rejects that challenge and attempts to enforce a reading of the contract that compels a party to violate the law, the courts retain their obligation to consider the public policy challenge on its merits. The Seventh Circuit, in the decision below, refused to hear Petitioner's challenge on antitrust grounds on its merits, choosing instead to give the arbitrators the final word on the lawfulness of their own ruling. At a minimum, the Court should clarify whether its statements in *W.R. Grace*, *Mitsubishi*, and *Vimar* reflect the proper role of the judiciary in enforcing arbitral awards that may violate fundamental public policy norms.

2. The Other Circuits Have Faithfully Applied This Court's Approach To Judicial Review Of Arbitral Awards For Compliance With Public Policy. All the other circuits to have confronted the issue agree that, even if an arbitrator considers

and rejects a public policy challenge to his interpretation of a contract, the losing party has a right to federal court review of the public policy issue at the award enforcement stage. "Once the public policy question is raised, [a court] must answer it by taking the facts as found by the arbitrator, but reviewing his conclusions de novo." *Iowa Elec. Light & Power Co.* v. *Local Union 204*, 834 F.2d 1424, 1427 (8th Cir. 1987); *MidMichigan Reg'l Med. Ctr.-Clare* v. *Professional Employees Div. of Local 97*, 183 F.3d 497, 504 (6th Cir. 1999) ("courts will not enforce a contract that they independently determine [has been interpreted by an arbitrator] to be contrary to public policy"); *Exxon Corp.* v. *Esso Workers' Union, Inc.*, 118 F.3d 841, 845 (1st Cir. 1997) ("the question of what public policy demands is within the judicial, not the arbitral, domain"), *abrogated on other grounds by Eastern Associated Coal Corp.* v. *United Mine Workers of Am., Dist. 17*, 531 U.S. 57 (2000); *Gulf Coast Indus. Workers Union* v. *Exxon Co., U.S.A.*, 991 F.2d 244, 248 n.5 (5th Cir. 1993) ("courts are the ultimate arbiters of public policy, not arbitrators"); *Exxon Shipping Co.* v. *Exxon Seamen's Union*, 993 F.2d 357, 360 (3d Cir. 1993) ("Once we identify a public policy, we must determine whether the arbitrator's award, as reflected in his interpretation of the agreement, violated that policy.").

The issue commonly arises in the labor arbitration context, in which a collective bargaining agreement permits an employer to fire an employee only for "just cause." Each time an arbitrator applies the "just cause" standard to a particular dismissal, he is effectively interpreting the "just cause" language of the contract either to cover or not to cover the circumstances presented. *Eastern Associated Coal Corp.* v. *United Mine Workers of Am., Dist. 17*, 531 U.S. 57, 61-62 (2000). Employers have claimed that reinstating the employee, as the union requests, would interpret the "just cause" language of the contract to require the employer to violate federal safety regulations. And, as the decisions

discussed below from the Second, Ninth, and Eleventh Circuits illustrate, the federal courts consider that public policy issue on its merits, even when the arbitrator has already considered the governing regulations and determined that they did not (or did) require the employer to dismiss the employee.[4]

In *International Brotherhood of Electrical Workers, Local 97* v. *Niagara Mohawk Power Corp.*, 143 F.3d 704 (2d Cir. 1998), an employee of a nuclear power plant had been dismissed by his employer after testing positive for cocaine. An arbitrator "examined at length" the federal regulations the power plant had cited concerning the public policy considerations at issue in the dispute. *Id.* at 709. The arbitrator ultimately ruled against the power plant and reinstated the employee. The power plant challenged the award on public policy grounds, and the Second Circuit independently reviewed the regulations at issue to determine whether they stated a public policy inconsistent with the arbitral award. *Id.* at 715-19.

Southern California Gas Co. v. *Utility Workers Union of America, Local 132*, 265 F.3d 787 (9th Cir. 2001), also involved a utility's dismissal of workers who had tested positive for drugs. The tests were administered pursuant to a federally mandated random testing program. *Id.* at 790. The parties disputed whether the tests had been administered in accordance with the program, and an arbitrator decided that they had not. *Id.* at 792. The arbitrator ordered the employees reinstated. The utility company challenged the award on public policy grounds, referring to a regulation that specifically required the company not to employ individuals

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[4] Indeed, this Court, in *Eastern Associated Coal*, 531 U.S. at 63-67, independently examined the employer's public policy defense to reinstatement even though the arbitrator had considered that issue in the first instance. Brief for Respondents at 3, *Eastern Associated Coal Corp.* v. *United Mine Workers of Am., Dist. 17*, 531 U.S. 57 (2000) (No. 99-1038).

who failed a federally mandated drug test. *Id.* at 795. Given that the arbitrator had already determined that the tests administered by the utility company did *not* comply with federal regulations, the opinion of the panel majority in this case would require a federal court to reject the utility company's public policy challenge without reaching its merits. But the Ninth Circuit, though affirming the arbitral award, specifically conducted its own review of the regulations to determine whether the drug tests had complied with federal requirements. *Id.* at 795-96.

Delta Air Lines, Inc. v. *Air Line Pilots Ass'n, International*, 861 F.2d 665 (11th Cir. 1988), involved the dismissal of a pilot for flying while intoxicated. The pilot was dismissed for violating both airline policy and federal regulations. *Id.* at 668. An arbitration panel reinstated the pilot. As the Eleventh Circuit viewed the arbitral ruling, the panel "ha[d] construed the collective bargaining agreement in such a manner that it appears that Delta has agreed to submit to arbitration the question as to whether it should authorize operation of aircraft by pilots while they are drunk." *Id.* at 671. Despite the fact that the arbitrators had been presented with the various legal bases that the airline asserted reflected a public policy against employment of pilots who have flown while intoxicated, see *Delta Air Lines, Inc.* v. *Airline Pilots Ass'n*, 686 F. Supp. 1573, 1575 (N.D. Ga. 1987), the Eleventh Circuit reviewed those materials *de novo* and found the arbitral award incompatible with public policy. 861 F.2d at 672-74.

The Seventh Circuit, in an opinion by a respected jurist, has stated a position that stands alone and conflicts with a standard of review adopted by the other circuits. This is precisely the situation in which review by this Court is warranted.

3. The Decision Below Threatens Effectively To Nullify The Public Policy Exception To Enforcement Of Arbitral Awards And Reflects Poor Arbitration Policy. The approach set forth

in *Grace*, *Mitsubishi*, and *Vimar*, and followed by the other circuits, should have led the Seventh Circuit to consider on its merits Petitioner's argument that the arbitral award was grossly anticompetitive and therefore that the interests of consumers required that it not be enforced. In accord with the approach outlined in these cases, Petitioner first tried to persuade the arbitrators that Abbott's proposed interpretation of the Dispute Resolution Agreement would cause the parties to violate the antitrust laws and Abbott to violate its consent decree with the FTC.[5] When the arbitration panel accepted Abbott's interpretation over Petitioner's opposition, based in part on public policy, Petitioner, again following the approach outlined above, asked the district court to "condemn[] the agreement as against public policy." *Mitsubishi*, 473 U.S. at 637 n.19.

The court of appeals rejected the course detailed by existing caselaw. Instead, the panel majority relied on the general, but here inapplicable, rule that when arbitrators decide antitrust claims, a court's review is limited. App. 4a-5a. That is certainly true when the parties have agreed to arbitrate an antitrust *claim*, seeking affirmative relief, brought by one party against another. *Mitsubishi*, 476 U.S. at 628-40. But that rule is not implicated when the antitrust issue is presented

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[5] Just this past April, this Court, in *PacifiCare Health Systems, Inc.* v. *Book*, 123 S. Ct. 1531 (2003), indicated that an arbitrator should be permitted, in the first instance, to consider whether an arbitration clause in a contract that prohibits the award of punitive damages in arbitration would prohibit the arbitrator from awarding treble damages under RICO. Nothing in *PacifiCare* suggests that submitting the issue to the arbitrator in the first instance would prevent a court, at the enforcement stage, from determining whether an arbitral decision to refuse to award treble damages based on the contract's prohibition on punitive damages violates public policy by frustrating the remedial purposes of RICO. If the Seventh Circuit's ruling stands, then *PacifiCare*'s rule requiring an arbitral ruling in those circumstances ensures that no court will be permitted to reach the underlying RICO issue.

as a public policy-based *defense* against the opposing party's proposed construction of a contract.

When raised as a *defense*, as Petitioner has done here, the antitrust issue presents a question within the well-settled meaning of the public policy exception to enforcement of arbitral awards: a court should not enforce an arbitral award that commands a party to violate the law. *Eastern Associated Coal*, 531 U.S. at 63; *Misco*, 484 U.S. at 42; *W.R. Grace*, 461 U.S. at 766. If Petitioner is correct, then the Dispute Resolution Agreement as interpreted by Abbott and the arbitrators violates the Sherman Act and an FTC consent decree. In turn, the arbitral award enforcing that agreement commands Petitioner to violate the Sherman Act. There is no similar possibility of a command to violate the law when the parties arbitrate an antitrust *claim*. Even an erroneous ruling that permits anticompetitive conduct to continue does not *compel* any violation of the law; it merely *permits* it.

The panel majority read *Mitsubishi* expansively to require courts to defer not only to an arbitrator's ruling on an antitrust *claim*, but also to an arbitrator's ruling that his own order does no violence to the antitrust laws. The panel found support for this expansive reading in the general rule that courts have only limited authority to review an arbitrator's ruling for legal errors. App. 4a. If allowed to stand, this line of analysis will vitiate the public policy exception in its entirety. As this Court has made clear, a party may seek to prevent enforcement of an arbitral award for violating public policy only when the policy is "well defined and dominant, and ... ascertain[able] 'by reference to the laws and legal precedents and not from general considerations of supposed public interests.'" *W.R. Grace*, 461 U.S. at 766. That is, public policy is revealed entirely through traditional materials of positive law – statutes, regulations, and court precedents. *Eastern Associated Coal*, 531 U.S. at 63. If courts must always defer slavishly to arbitrators' analyses of positive law, even in the context of public policy challenges to arbitral

awards themselves, then there is nothing left of the public policy exception, which is supposed to restrict an arbitrator's power. The panel majority's analysis thus has the effect of reading the public policy exception to enforcement of arbitral awards out of the New York Convention. New York Convention, art. V, § 2(b) (stating enforcement should be refused where "recognition or enforcement of the award would be contrary to the public policy of [the court's] country"), *reproduced in* 9 U.S.C. § 201 note.

Thwarting the public policy exception to enforcement of arbitral awards is not only contrary to the New York Convention and the precedents discussed above, but is also unsound arbitration policy. As an initial matter, because arbitration agreements are contracts, they should be interpreted and applied consistent with the parties' intent. *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279, 294 (2002). It is hardly reasonable to assume that parties intend to insulate from judicial review not only the arbitrator's interpretation of the contract, but also an order that compels a violation of positive law.

Further, this Court repeatedly has emphasized the federal policy favoring arbitration of disputes. *Gilmer* v. *Interstate/Johnson Lane Corp.*, 500 U.S. 20, 25 (1991); *Moses H. Cone Mem'l Hosp.* v. *Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983). Arbitration provides a speedy and efficient means of resolving disputes, and helps relieve the burden on the court system. *Prima Paint Corp.* v. *Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 (1967). Depriving a party of the opportunity to obtain court relief if an arbitrator's erroneous legal analysis leads the arbitrator to order that party to violate the law places an added cost, a potentially large cost, on every arbitration clause: the potential for an unreviewable order to violate the law. As the panel majority itself recognized, while Petitioner and Abbott are bound to respect the arbitrators' conclusion that the arrangement is lawful, others are not. App. 5a-6a. Either or both of Petitioner and Abbott are, as a

result of the arbitral ruling which the Seventh Circuit has deemed unreviewable, exposed to potentially costly antitrust suits. This additional cost can serve only to discourage use of the arbitration process by contracting parties, contrary to the federal policy favoring arbitration.

* * * *

A badly divided Seventh Circuit has staked out a provocative position concerning the relationship between arbitrators and courts with respect to the protection of public policy. Notwithstanding prior statements of this Court indicating that such issues are ultimately for the courts to decide, the court below concluded that judicial deference to arbitration decisions extends even to determining the validity of those decisions measured against the demands of public policy. Other circuits would not have refused to consider Petitioner's antitrust arguments on their merits. Indeed, the ruling below renders impotent the command of the New York Convention not to enforce awards that conflict with public policy, and the ruling will undercut the willingness of contracting parties to opt for arbitration. The court of appeals has cried out for this Court to review its decision; the Court should accept that invitation.

CONCLUSION

The petition for writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

UNITED STATES COURT OF APPEALS
SEVENTH CIRCUIT

No. 02-2039

BAXTER INTERNATIONAL, INCORPORATED,
Plaintiff-Appellant,

v.

ABBOTT LABORATORIES,
Defendant-Appellee.

Argued Oct. 29, 2002
Decided Jan. 16, 2003

Before CUDAHY, COFFEY, and EASTERBROOK, Circuit Judges.

EASTERBROOK, Circuit Judge.

Baxter International invented sevoflurane in the 1960s. This substance, a gas at room temperature, has good anesthetic properties. But it was too difficult and costly to produce commercially until the early 1980s, when Baxter devised an efficient process for its manufacture. Baxter obtained two process patents, the latter of which expires in December 2005. But the anesthetic gas still could not be sold in the United States unless it first received the FDA's approval, and Baxter was not willing to bear the costs of the required medical testing. So in 1988 it granted to Maruishi Pharmaceutical Company, of Japan, an exclusive worldwide license to practice the sevoflurane process patents Baxter owned or was pursuing. Maruishi obtained approval to sell the anesthetic in Japan, where it was a great success, as it has

become in other nations since. This suggested that it would be worth obtaining the FDA's approval to sell in the United States. Abbott Laboratories took a sublicense from Maruishi in 1992, obtained the FDA's approval after spending approximately $60 million on testing, and in 1995 began selling sevoflurane in the United States. Maruishi remains the sole manufacturer under the Baxter patents; Abbott resells sevoflurane that it purchases from Maruishi, which pays Baxter a royalty based on its total sales. Today sevoflurane is the best-selling gas used for anesthesia in the United States, with approximately 58% of sales. Desflurane holds 35% of this market, and isoflurane accounts for almost all of the remaining sales. Isoflurane is not protected by any patent and sells for less, but it is slower in both onset and recovery and has an irritating taste and smell. Desflurane likewise has an annoying smell and aftertaste, though its properties otherwise are comparable to sevoflurane—which therefore has become the anesthetic of choice and commands a premium price.

Sevoflurane's success gave rivals an incentive to invent around Baxter's process patents. Ohio Medical Associates (now known as Ohmeda) set out in 1997 to do just this. In 1999 Ohmeda obtained a patent for a new way of making sevoflurane, distinct from Baxter's process but equivalently cheap and effective. It planned to introduce a rival sevoflurane anesthetic, which it could do by filing a "me too" application with the FDA. Ohmeda could receive approval without costly tests just by showing that the finished product is identical to Abbott's.

Before Ohmeda could bring sevoflurane to market, it was acquired (in 1998) by Baxter—which decided to proceed with Ohmeda's plans and compete with the sevoflurane made by Maruishi and sold in the United States by Abbott. Baxter concluded that it would make more from selling Ohmeda-process sevoflurane than it would lose in reduced royalties from Maruishi for Baxter-process sevoflurane. Abbott, which

contends that it has spent more than $1 billion to commercialize sevoflurane (including distribution of equipment for administering the drug and marketing to alert anesthesiologists to its benefits) did not welcome competition before the expiration of the Baxter patents. Abbott initiated arbitration under the Baxter-Maruishi agreement (to which it had become a party in 1992) and the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, [1970] 21 U.S.T. 2517, T.I.A.S. No. 6997, implemented by 9 U.S.C. §§ 201-08. The agreement specifies a multi-national tribunal, which consisted of a U.S. attorney, a Spanish attorney, and a Japanese law professor.

Abbott contended that Baxter's sale of Ohmeda-process sevoflurane before the Baxter patents expired would violate the exclusivity term of the license; Baxter replied, first, that the license does not explicitly forbid Baxter itself from competing with Maruishi (in other words, that exclusivity means only that Baxter can not issue any other licenses), and, second, that if the license does forbid Baxter from competing, then it violates U.S. antitrust law, particularly § 1 of the Sherman Act, 15 U.S.C. § 1, and is unenforceable. The arbitrators ruled against Baxter on both issues. The tribunal held that the license is exclusive in the strong sense and that any reduction in competition is attributable to Baxter's decision to purchase the competing Ohmeda process while bound by this promise not to compete with its licensee. On cross suits filed by Abbott and Baxter, the district judge then directed Baxter to comply with the award, rejecting its contention that the license, as construed by the tribunal, violates the Sherman Act or the public policy of the United States. The judge observed that competition from desflurane, isoflurane, and sevoflurane made by any other process (for the sevoflurane molecule is unpatented) is unaffected. 2002 WL 467147, 2002 U.S. Dist. LEXIS 5475 (N.D.Ill. Mar. 27, 2002).

Baxter argues at length in this court that the Baxter-Maruishi license, construed to keep Ohmeda-process sevoflurane off the U.S. market until 2006, is a territorial allocation unlawful *per se* under § 1 of the Sherman Act. But the initial question is whether Baxter is entitled to reargue an issue that was resolved by the arbitral tribunal. We think not; a mistake of law is not a ground on which to set aside an award. See *George Watts & Son, Inc. v. Tiffany & Co.*, 248 F.3d 577 (7th Cir.2001). Section 207 says that "[t]he court shall confirm the award unless it finds one of the grounds for refusal or deferral of recognition or enforcement of the award specified in the said Convention." Legal errors are not among the grounds that the Convention gives for refusing to enforce international awards. Under domestic law, as well as under the Convention, arbitrators "have completely free rein to decide the law as well as the facts and are not subject to appellate review." *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145, 149, 89 S.Ct. 337, 21 L.Ed.2d 301 (1968). "Courts thus do not sit to hear claims of factual or legal error by an arbitrator". *United Paperworkers v. Misco, Inc.*, 484 U.S. 29, 38, 108 S.Ct. 364, 98 L.Ed.2d 286 (1987).

Arbitrators regularly handle claims under federal statutes. See, e.g., *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 109 S.Ct. 1917, 104 L.Ed.2d 526 (1989) (claims under the Securities Act of 1933); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 107 S.Ct. 2332, 96 L.Ed.2d 185 (1987) (claims under the Securities Exchange Act of 1934 and the Racketeer Influenced and Corrupt Organizations Act); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 94 S.Ct. 2449, 41 L.Ed.2d 270 (1974) (international arbitration of claims under the Securities Exchange Act of 1934). We do not see any reason why things should be otherwise for antitrust issues—nor, more importantly, does the Supreme Court, which held in *Mitsu-*

bishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 105 S.Ct. 3346, 87 L.Ed.2d 444 (1985), that international arbitration of antitrust disputes is appropriate.

Mitsubishi did not contemplate that, once arbitration was over, the federal courts would throw the result in the waste basket and litigate the antitrust issues anew. That would just be another way of saying that antitrust matters are not arbitrable. Yet this is Baxter's position. It wants us to disregard the panel's award and make our own decision. The Supreme Court's approach in *Mitsubishi* was different. It observed (473 U.S. at 639 n. 21, 105 S.Ct. 3346):

> The utility of the Convention in promoting the process of international commercial arbitration depends upon the willingness of national courts to let go of matters they normally would think of as their own. Doubtless, Congress may specify categories of claims it wishes to reserve for decision by our own courts without contravening this Nation's obligations under the Convention. But we decline to subvert the spirit of the United States' accession to the Convention by recognizing subject-matter exceptions where Congress has not expressly directed the courts to do so.

Starting from scratch in court, as Baxter proposes, would subvert the promises the United States made by acceding to the Convention.

According to Baxter, there is a difference between arbitrating an antitrust issue (the subject of *Mitsubishi*) and *creating* one—which it accuses these arbitrators of doing. If the tribunal had construed the Baxter-Maruishi agreement differently, there would have been no antitrust problem. Baxter relies on the observation in *George Watts* that arbitrators are not allowed to command the parties to violate rules of positive law. That's true enough, but *whether* the tribunal's construction of the Baxter-Maruishi agreement has

that effect was a question put to, and resolved by, the arbitrators. They answered no, and as between Baxter and Abbott their answer is conclusive. This is a point anticipated in *Mitsubishi,* which observed (*id.* at 638, 105 S.Ct. 3346): "While the efficacy of the arbitral process requires that substantive review at the award-enforcement stage remain minimal, it would not require intrusive inquiry to ascertain that the tribunal took cognizance of the antitrust claims and actually decided them." The arbitral tribunal in this case "took cognizance of the antitrust claims and actually decided them." Ensuring this is as far as our review legitimately goes.

Treating Baxter as bound (*vis-à-vis* Abbott) by the tribunal's conclusion that the license (as construed to provide strong exclusivity) is lawful does not condemn the public to tolerate a monopoly. If the three-corner arrangement among Baxter, Maruishi, and Abbott really does offend the Sherman Act, then the United States, the FTC, or any purchaser of sevoflurane is free to sue and obtain relief. None of them would be bound by the award. As far as we can see, however, only Baxter is distressed by the award—and Baxter, as a producer, is a poor champion of consumers. See *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 110 S.Ct. 1884, 109 L.Ed.2d 333 (1990); *Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104, 107 S.Ct. 484, 93 L.Ed.2d 427 (1986); *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 97 S.Ct. 690, 50 L.Ed.2d 701 (1977).

What relief the Antitrust Division, the FTC, or a consumer would obtain, if there is an antitrust problem, is an interesting question. Baxter thinks that the solution should be an order allowing it to sell Ohmeda-process sevoflurane. It wants to take its acquisition of Ohmeda as given and ask what consequences it has for exclusivity under the Baxter-Maruishi agreement. Yet this is anachronistic. The Baxter-Maruishi agreement came first, and its exclusivity rule was a lawful ancillary agreement designed to induce Maruishi and its

sublicensees to make the investments needed to bring the new drug to market. See generally *Polk Bros., Inc. v. Forest City Enterprises, Inc.*, 776 F.2d 185 (7th Cir.1985); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210 (D.C.Cir.1986) (Bork, J.). At the time Baxter acquired Ohmeda it was obliged by contract to refrain from producing sevoflurane until 2006. (This is how the tribunal understood the Baxter-Maruishi agreement, and a court must accept this interpretation.) So if there is an antitrust problem, it lies in the acquisition—and the remedy would be divestiture of the Ohmeda process patent. Baxter can achieve that outcome on its own. Baxter, which can solve unilaterally any antitrust problem, is in no position to insist that the burden of solution fall on Abbott by depriving it of the benefit of the exclusive Baxter-Maruishi license. Why should a decision Baxter made in 1998 reduce the rights Abbott enjoys under a promise Baxter made to Maruishi in 1988? But it is unnecessary to pursue this line of argument. All that matters today is that the arbitrators have concluded that the antitrust laws (and Baxter's related arguments, which we need not address) do not diminish Abbott's contractual rights—and that decision is conclusive between these parties.

AFFIRMED

CUDAHY, Circuit Judge, dissenting.

To understand fully why the majority's enforcement of this dubious arbitration award is misguided, a brief synopsis of the background material not fully described by the majority is essential. In 1983 and in 1988 Baxter gave options to Maruishi to license patents covering the one-step process of manufacturing sevoflurane. By 1992, when negotiations with Abbott concerning the introduction of sevoflurane in the United States were undertaken, Baxter's product and method-of-use patents for sevoflurane had expired. Arbitration Transcript at 675-83 ("Arb.Tr."). Hence, the only patents that Baxter could license to Maruishi and that Maruishi could in turn sublicense to Abbott were those covering the one-step manufacturing *process,* which were still in effect. In its negotiations with Baxter, Maruishi considered attempting to obtain a covenant not to compete not only with respect to the one-step process but also as to sevoflurane itself, but instead turned its attention elsewhere. Maruishi concluded that the exclusive license for the one-step process and related intellectual property was "sufficient protection." *See* Arb. Tr. at 523-24. The 1992 negotiations with Abbott dealt only with the one-step process. Arb. Tr. at 386-91.

In 1992, when sublicensing to Abbott was negotiated, two distinct sets of agreements were involved in the negotiations. First, there were the Sevoflurane Agreements establishing the terms of the licenses, and granting exclusive rights to Maruishi and to Abbott to manufacture sevoflurane under the one-step patent, to all improvements on the one-step patents and to all technology and confidential proprietary information ("know-how") acquired during the development of the one-step process. Next, all the parties entered into a Dispute Resolution Agreement (DRA), first, to ensure that in the event of a dispute commercialization of sevoflurane would go forward and, second, to provide a mechanism (arbitration) for resolving disputes arising from the Sevoflurane Agreements

that would arguably impair what the parties referred to as the "Original Commercial Relationship" (OCR). The arbitrators were instructed by the DRA to attempt to maintain this Original Commercial Relationship—an "unusual" concept. Appellant's Br. at 9.

By the late 1990s, Ohmeda had developed and patented a different, *three-step* process to make sevoflurane suitable to be marketed as a generic drug. Subsequently, Baxter acquired Ohmeda. Faced with the threat of generic competition—always anticipated, but now apparently to be undertaken by Baxter—Abbott sought arbitration. The arbitration panel conceded that the Baxter-Maruishi *licensing* agreement would not preclude Baxter's offering generic competition because this licensing agreement covered only the one-step manufacturing process, which bore no relation to the three-step process. But a two-member majority of the panel found that, under the Dispute Resolution Agreement invoking the Original Commercial Relationship, Baxter's proposed sales of generic sevoflurane could be enjoined because they would reduce Abbott's revenues below monopoly levels, even though the expectation of generic competition was nothing new. The third member of the arbitral panel (the only American) dissented since he concluded that the arbitrators were not authorized to act independent of the licensing agreement itself. The majority also found a breach of an Illinois state duty of good faith, which the dissenting arbitrator thought specious.

The majority upholds the arbitration award here by declaring that, once the arbitrators have spoken to the antitrust issues and in effect commanded the parties to violate the Sherman Act, the courts have no business intervening. Of course, the doctrine that requires extreme deference by the courts to arbitration awards is based on the theory that the parties to a contract may cede broad, almost unlimited, power to an arbitration panel to interpret their agreement. *See First*

Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 115 S.Ct. 1920, 131 L.Ed.2d 985 (1995); *see also IDS Life Ins. Co. v. Royal Alliance Assoc., Inc.*, 266 F.3d 645, 649 (7th Cir.2001) ("Within exceedingly broad limits, the parties to an arbitration agreement choose their method of dispute resolution and are bound by it however bad their choice appears to be either ex ante or ex post."). In fact, the arbitrators function almost as agents of the parties to extend their deal to cover unforeseen circumstances. *See E. Associated Coal Corp. v. United Mine Workers of America*, 531 U.S. 57, 62, 121 S.Ct. 462, 148 L.Ed.2d 354 (2000) (telling courts to "treat the arbitrator's award as if it represented an agreement between [the parties] as to the proper meaning of the contract's words."); *EEOC v. Indiana Bell Tel. Co.*, 256 F.3d 516, 522 (7th Cir.2001) ("The arbitrator acts on their (joint) behalf, with whatever authority the contract bestows. The resulting award is effectively the parties' joint decision."). All this rests on the proposition that the parties are free to adjust rights and liabilities *among themselves* as they see fit and through the instrumentality of arbitration to follow wherever the situation may demand. In this bilateral context a commitment to deference cannot be questioned.

But other considerations enter the mix when the issue becomes a matter of the arbitrators', in interpreting a statute, commanding the parties to break the law or to violate clearly established norms of public policy.[1] In the case before us, the arbitrators have instructed Abbott and Baxter (by imposing on

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[1] As the majority notes, the present case is governed by the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 21 U.S.T. 2517, T.I.A.S. No. 6996, implemented by 9 U.S.C. §§ 201 *et seq.* ("Convention"). 9 U.S.C. § 207 commands a court to enforce an arbitration award under the Convention unless one of the grounds for refusal to enforce found in the Convention is present. Article V(2)(b) of the Convention allows a court to refuse to enforce an arbitration award when "recognition or enforcement of the award would be contrary to the public policy of that country."

Baxter a broad covenant not to compete with respect to sales of sevoflurane itself) to effect a horizontal allocation of markets, a clear violation of the Sherman Act. Under the arbitral decision, Abbott is granted a monopoly [2] in the sale of sevoflurane in the United States.

For some considerable time not long in the past, the law of the land was that antitrust disputes were not arbitrable. *See Am. Safety Equip. Corp. v. J.P. Maguire & Co.*, 391 F.2d 821 (2d Cir.1968); *Applied Digital Tech., Inc. v. Continental Cas. Co.*, 576 F.2d 116 (7th Cir.1978). Claims made under the Sherman Act were not merely private claims, but were quasi-public claims designed to protect the rights of consumers and the public at large. *Applied Digital Tech.*, 576 F.2d at 117. Since more than merely the rights of the parties were at issue, the agreement of the parties to arbitrate could not supersede the public's presumed interest in a judicial resolution of antitrust claims.

The growing fondness for arbitration, however, eventually eliminated the prohibition on submitting antitrust matters to arbitration. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 105 S.Ct. 3346, 87 L.Ed.2d 444 (1985), did not purport to directly overturn the doctrine that domestic antitrust claims could not be arbitrated, but subsequently, the Supreme Court in dicta and most of the Courts of Appeal considering the issue have interpreted *Mitsubishi* as placing antitrust and other statutory claims within the ambit of arbitration. *See, e.g., Gilmer v. Interstate/ Johnson Lane Corp.*, 500 U.S. 20, 28, 111 S.Ct. 1647, 114 L.Ed.2d 26 (1991) ("The Sherman Act, the Securities Exchange Act of 1934, RICO, and the Securities Act of 1933

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[2] There is no dispute that Baxter's Ohmeda is the only generic competitor in the sevoflurane market for the foreseeable future, nor is there a dispute that the arbitral decision's prohibition on the sale of generic sevoflurane by Baxter preserves monopoly prices and levels of output of Abbott's sevoflurane product.

all are designed to advance important public policies, but, as noted above, claims under those statutes are appropriate for arbitration."); *Seacoast Motors of Salisbury, Inc. v. Daimler-Chrysler Motors Corp.*, 271 F.3d 6 (1st Cir.2001); *Kotam Elecs., Inc. v. JBL Consumer Prods., Inc.*, 93 F.3d 724 (11th Cir.1996); *Sanjuan v. Am. Bd. of Psychiatry & Neurology, Inc.*, 40 F.3d 247 (7th Cir.1994); *Nghiem v. NEC Elec., Inc.*, 25 F.3d 1437 (9th Cir.1994); *Swensen's Ice Cream Co. v. Corsair Corp.*, 942 F.2d 1307 (8th Cir.1991).

The present case is a good example of the extent to which arbitration has come to pervade the legal culture. First, the parties here constructed an elaborate, pre-dispute arbitration agreement that not only served to regulate the licensing agreement itself, but also, in an extraordinary spasm of creativity during the arbitration, generated a new and seemingly boundless cause of action, entirely separate from the license itself, under which the parties could presumably proceed. Then, during the arbitral process, Baxter submitted to the arbitrators the supplemental argument [3] that, if the arbitrators pursued what eventually did become their line of decision, they would be commanding unlawful conduct under

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[3] It is an important distinction that this rather meta-juridical antitrust claim "decided" by the arbitrators was not a simple claim by Baxter against Abbott, but rather a request by Baxter that the arbitrators step back and consider the larger implications of their underlying decision. This distinction becomes clear when one recognizes that this issue could simply have been ignored by the arbitrators and considered for the first time in the district court—the arbitrators' interpretation of the license and the DRA did not involve antitrust issues. But, if Baxter had not raised the antitrust issue during arbitration, it would have risked being met with a defense of waiver to consideration of the issue here. Yet, on the other hand, Baxter's position here might well have been strengthened if it had chosen not to bring the question forward during arbitration and thereby armed Abbott with the (dispositive, as it turns out) argument for deference to the arbitration award.

the Sherman Act. And finally, neither Baxter nor Abbott contend that arbitration was inappropriate for resolution of the antitrust claim.

Now, the majority has taken the process one giant step further and has found that *Mitsubishi* not only allows submission of statutory and antitrust claims to arbitration, but denies our prerogative to refuse to enforce awards that command unlawful conduct.[4] The deciding circumstance, according to the majority, is that the question was put to, and decided by, the arbitrators themselves. Maj. Op. at 832 ("That's true enough, [that arbitrators are not allowed to command unlawful conduct,] but *whether* the construction of the Baxter-Maruishi agreement has that effect was a question put to, and resolved by, the arbitrators. . . . [A]s between Baxter and Abbott, their answer is conclusive."). Therefore, under the majority's analysis, the rule that unlawful conduct cannot be commanded by arbitrators is consumed by the exception that, if the arbitrators themselves say that what they have commanded is not unlawful, then "their answer is conclusive."

This cannot be correct. While *Mitsubishi* and its progeny make clear that the choice of the arbitral forum is to be respected, they do not confer on the arbitrators a prerogative to preemptively review their own decisions and receive deference on that review in subsequent judicial evaluations.[5]

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[4] The Convention itself provides grounds for refusing to confirm an award under "public policy" principles. This circuit has recognized grounds (under the Federal Arbitration Act) for refusing to confirm if an arbitration panel acts in manifest disregard of the law, or, as otherwise viewed, if the arbitrators' decision commands a party to act unlawfully. *George Watts & Son, Inc. v. Tiffany & Co.*, 248 F.3d 577 (7th Cir.2001). Rather than repeatedly referring to the applicable tests, I will simply refer to "unlawful conduct."

[5] It is clear that the arbitrators were doing exactly that—reviewing their own decision—and not deciding issues of law necessary to interpret the

The majority is way off-base when it says that Baxter seeks merely to have us disregard the panel's decision and "throw the result in the waste basket." Maj. Op. at 832. Instead, we are performing exactly the traditional function of judicial review properly assigned only to us.

Therefore, I do not think we can simply note the arbitration panel's resolution of the antitrust issue and consider our work done. Instead, we must fulfill our judicial responsibilities and examine the effect of the outcome commanded by the arbitral award.[6] This means that we have to determine whether, going forward, the horizontal restraint on Baxter's competing with Abbott in the sevoflurane market violates the Sherman Act.

Sometimes, of course, a horizontal restraint is a necessary part of an endeavor that, in the whole, benefits consumers. *Nat'l Collegiate Athletic Ass'n v. Bd. of Regents of Univ. of Oklahoma*, 468 U.S. 85, 101, 104 S.Ct. 2948, 82 L.Ed.2d 70 (1984). That is the claim here—that Abbott would not have undertaken to launch sevoflurane commercially had it not been guaranteed against all competition by Baxter. Yet it is conceded that there was no express covenant not to compete.[7]

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various agreements. The panel's "decision" on the antitrust issues is that "[i]t considers that no illegality results from the interpretation of the Sevoflurane Agreements in this Award." Supp.App. at 18-19.

[6] My analysis takes place in the context that the meaning of the Sevoflurane Agreements, as interpreted by the arbitrators, is not contested by Baxter. Therefore, although the arbitrators' findings seem a bit far-fetched to me, I take as a given that the DRA contains a broad, if implied, covenant not to compete that prohibits Baxter from competing with Abbott in any way in the sevoflurane market. This, of course, does not respond to the issue of lawfulness, which is the subject of my substantive analysis.

[7] The majority bolsters its deference argument by glossing over some significant nuances in the various Baxter-Maruishi-Abbott agreements and the arbitral decision. The arbitrators did not hold "that the license is exclusive in the strong sense." Maj. Op. at 831. In fact, the arbitrators

Baxter gave an exclusive license to the one-step process but no guarantee against competition in sevoflurane produced by some other process. The absence of an express covenant not to compete strongly suggests that such a covenant could not have been the *sine qua non* of Abbott's launching sevoflurane in the United States market.

The majority unquestioningly accepts the contrary proposition of Abbott, that this broad implied noncompete covenant was "a lawful ancillary agreement designed to induce Maruishi and its sublicensees to make the investments needed to bring the new drug to market." Maj. Op. at 823. First, as I have already noted, Maruishi has never argued that it needed, or believed it had received, the broad noncompete found by the arbitrators. Second, this statement begs the question of what possible added incentive Abbott could have received from this additional guarantee of monopoly above and beyond the scope of the one-step patent.[8] By agreeing to

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found that the license, which is limited solely to the one-step process and all associated know-how and technology, was not violated in any way by Baxter's actions regarding the three-step process. Supp.App. at 13-14. The "strong" noncompete was *implied from the DRA*, which the arbitration panel found contained its own independent cause of action and provided relief to Abbott for *any* conduct by Baxter that reduced the monopoly revenue Abbott would otherwise receive under the one-step licenses. In theory, under the broad language of the arbitral award, even if Baxter invented and brought to market (before 2005) a completely new and different inhalable anesthetic that competed with sevoflurane and reduced Abbott's revenues from it, Baxter would be in violation of the DRA and enjoined from any manufacture and sale. See Supp.App. at 15, ¶¶ 25, 26.

[8] I note briefly the questions raised by the Fourth Circuit's decision in *Compton v. Metal Products, Inc.*, 453 F.2d 38 (4th Cir.1971). In that case, a patentee licensed its patented technology together with a broad (express) noncompete that went far beyond the scope of the patented technology. The court found this agreement not to compete an unlawful restraint of trade. I am unconvinced by the district court's efforts to distinguish *Compton* from the present case on the basis of the degree to

completely exclude itself from any activity in the sevoflurane market that involved the one-step process, the know-how related to the one-step process or any "improvement" on the technology or know-how of the one-step process patents, Baxter relegated itself to a position identical to that of the other potential competitors that were anticipated by Abbott. Abbott had the incentive to commercialize sevoflurane in the United States with the knowledge that competitors like Ohmeda were lying in wait to "free-ride" on Abbot's regulatory approval and commercialization efforts. There is no reason why Abbott would lose any of its incentive if Baxter were added to the list of potential competitors (or would gain incentive if Baxter were excluded from the list), so long as Baxter remained excluded from one-step competition and was barred from using any of the know-how and technology associated with its development of the one-step process.[9] I do not think that there could rationally have been any pro-competitive effect from the enhanced noncompete implied by the arbitrators.

Arbitration proceedings aside, and given that a covenant not to compete was not essential to Abbott's market

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which Baxter was restricted. *Abbott Labs. v. Baxter Intern., Inc.*, 2002 WL 467147, *9 (N.D.Ill. March 27, 2002). The point of *Compton* is that restraints on competition beyond the scope of the licensed patented technology are unlawful. *Id.* at 45 ("We think that by agreeing to restrictions on his own competition which he could not compel of others, the patentee has extended the monopoly granted by the patent laws beyond its legal bounds."). This agreement to restrictions that extend and enhance the scope of the patent monopoly is also what is objectionable here.

[9] In fact, an argument can be made that Baxter was disadvantaged compared to other competitors by virtue of its agreement with Abbott and association with the one-step process. Baxter would face, as it did in the arbitration in the present case, the hurdle of showing that it did not succumb to the temptation to use any of its existing knowledge and technology base, a hurdle not faced by an outside competitor.

development, Abbott and Baxter could not lawfully agree to this arrangement without violating the Sherman Act, and I fail to see why a panel of arbitrators, on behalf of the parties, can interpret a prior agreement of these parties to reach the same unlawful result.

It is, of course, not the interests of the parties themselves that are primarily at stake in the outcome of this arbitration. Instead the interest of the consuming public is at stake. That public faces higher prices and a constrained supply of sevoflurane as a result of Abbott's monopoly, conferred by the arbitrators. When public rights are at stake, there is good reason to be more reluctant to defer totally to the arbitrators, since they are acting as delegates of the private parties, not of the consuming public. Too deferential an attitude by the courts when the rights of the consuming public are at stake can severely undermine the foundations of our economy. For there can be little doubt that granting Abbott a monopoly to produce sevoflurane in the United States will raise prices and restrict supply. And applying the analysis of the majority to arbitration awards yet to come will open a royal detour around the antitrust laws.

Nor would a denial of the remedy imposed by the arbitrators result in a real loss to Abbott, since Abbott admitted at the arbitration hearing that it had anticipated and planned for generic competition and had specifically anticipated competition from Ohmeda. Arb. Tr. at 323-25; Supp.App. at 19. In fact, Abbott negotiated with Maruishi provisions that would "account[ ] for the downsides of generic competition." Arb. Tr. at 323. The purchase of Ohmeda by Baxter produced a windfall for Abbott whereby Abbott was able to manipulate the arbitration to its advantage and escape the competition it had earlier anticipated.

It is not my role to critique the arbitration decision—however flawed—except in this case to object to its anti-competitive outcome, which orders the parties to violate the

antitrust laws. The interest of consumers was not represented on the arbitration panel and the panel's decision ignored consumer interests. Defense of public interests is sometimes better fulfilled by courts than by arbitration panels.

Nor am I much reassured by the substitute antitrust enforcement possibilities mentioned by the majority. It is conceivable that the Federal Trade Commission or the Justice Department might attack Abbott's monopoly conferred by the arbitrators or that another competitor might surface to provide competition from a generic sevoflurane manufactured by some process yet to be invented, but these possible sources of law enforcement or of competition are all hypothetical. I know of no authority for the theory that the existence of hypothetical sources of antitrust enforcement or of competition can be a defense to an agreement violative of the antitrust laws or to an arbitration award imposing such an agreement.

So while I agree with the majority that antitrust claims are arbitrable, and I also agree that the grounds for refusing to enforce an arbitration award are limited, I do not agree that there is support in the law for the majority's excision of antitrust arbitration from the general framework of judicial review that prohibits an arbitration panel's award from commanding illegal conduct. And in the case before us, the arbitration panel's ruling granting Abbott a monopoly in the United States sevoflurane market commands illegal conduct on the part both of Baxter and Abbott and is unenforceable.

I would remand with instructions not to enforce the arbitral award, and I therefore respectfully DISSENT.

APPENDIX B

UNITED STATES DISTRICT COURT,
N.D. ILLINOIS, EASTERN DIVISION

Nos. 01 C 4809, 01 C 4839

ABBOTT LABORATORIES,
Petitioner,

v.

BAXTER INTERNATIONAL INC.,
Respondent.

BAXTER INTERNATIONAL, INC.,
Petitioner,

v.

ABBOTT LABORATORIES,
Respondent.

March 27, 2002.

GUZMAN, J.

Pending are the parties cross motions for summary judgment pursuant to Fed.R.Civ.P. 56. For the reasons set forth below Petitioner Abbott Laboratories' motion is granted and Respondent Baxter International, Inc.'s motion is denied. Abbott's motion to strike the affidavits submitted by Baxter is granted. The final award dated June 15, 2001 and issued on June 22, 2001 is hereby confirmed.

BACKGROUND FACTS

Sevoflurane is a fluorine-based inhalation anaesthetic first developed by Baxter International, Inc. ("Baxter") scientists

in the mid-1960s and since then has been subject to a product patent and various process patents in the United States and elsewhere. Baxter succeeded in developing an efficient process for the production of sevoflurane in which a chemical called HFIP is mixed with formaldehyde and hydrogen fluoride in the presence of sulphuric acid and heat. This method of production, known as the "one-step process," is covered by two U.S. patents, Patent No. 4,250,334 and 4,469,898 ("the '334 and '898 patents"), assigned to Baxter which expire in 2001 and 2004.

During the 1980's Baxter decided to license it's rights to market sevoflurane, rather than market it directly. It developed a relationship with Maruishi, a Japanese pharmaceutical company, who commercially developed sevoflurane with great success in Japan. In 1983, Baxter gave Maruishi an option to license, on an exclusive basis, Baxter's sevoflurane patents in Japan, Korea, the Philippines and Taiwan. In 1988, Baxter gave Maruishi a further option to acquire worldwide rights to all of Baxter's then-existing sevoflurane patents.

Abbott Laboratories ("Abbott") and Maruishi then began discussions of a possible arrangement for Abbott to market sevoflurane in places where Maruishi did not do business. Maruishi began negotiations with Abbott and Baxter to develop a new agreement that would enable Maruishi to sell sevoflurane to Abbott for resale around the world. On September 3, 1992, Baxter and Maruishi signed a Patent and Know-How License agreement (hereafter Baxter/Maruishi Agreement).

Clause 2.1 of the Baxter/Maruishi Agreement granted licences in the following terms:

> 2.1 Baxter hereby grants to Maruishi an exclusive license even as to Baxter under the Licensed Patents and any improvements thereon to make, use, have made, sell, and have sold Sevoflurane and HFIP throughout the

'Territory' with rights to sublicense. The 'Territory' shall mean the world, excluding Japan, North and South Korea, and the People's Republic of China exclusive of Hong Kong. 'Sevoflurane and HFIP' shall mean Sevoflurane and HFIP manufactured using a process that but for the license granted therein would infringe one or more of the Licensed Patents.

2.2 Baxter hereby grants to Maruishi an exclusive license even as to Baxter under the Japanese Patents and any improvements thereon to make Sevoflurane and HFIP in Japan, and to sublicense Central Glass to make Sevoflurane and HFIP in Japan, for sale exclusively to Maruishi for resale by Maruishi in Japan exclusively to Abbott in Japan for resale by Abbott throughout the Territory.

Clause 1.2 defined 'Licensed Patents' as various patents relating to HFIP and/or Sevoflurane listed in Exhibit A to the Baxter/Maruishi Agreement. These included the '334 and '898 Patents, but not the '239 Patent. The '239 patent was previously owned by Ohmeda and recently acquired by Baxter and involves a three-step process to manufacture a generic sevoflurane.

The Baxter/Mariushi Agreement also contained a Know-How License in Clause 2.3:

2.3 Baxter hereby grants Maruishi an exclusive license even as to Baxter to use the Know-How and any improvements thereon to make, use, have made, sell and have sold Sevoflurane and HFIP in the Territory, with rights to sublicense, and an exclusive license even as to Baxter with rights to sublicense to Central Glass to use the Know-How and any improvements thereon to make and use Sevoflurane and HFIP in Japan for sale

exclusively to Maruishi in Japan and resale by Maruishi exclusively to Abbott in Japan for resale by Abbott throughout the territory.

'Know-How' was defined in Clause 1.1 as follows:

1.1 Prior to January 1983, Baxter developed a new inhalant anaesthetic known as 'Sevoflurane' through the Phase I clinical trial stage in accordance with the guidelines of the United States Food and Drug Administration ('FDA') and, as a part of such development, acquired confidential proprietary information ('Know-How'). Baxter has supplied Maruishi with all Know-How relating to Sevoflurane and/or HFIP (an immediate form of Sevoflurane), including physico-chemical date, stability profiles, toxicity studies, mutagenicity studies, metabolic and pharmaco-kineric data, and copies of all FDA correspondence, which have been collected by Baxter.

Section 3 of the Baxter/Maruishi Agreement provided for payments for the license granted by Baxter:

3.0 Payments

3.1 for the Section 2 license grant, Maruishi shall make four (4) nonrefundable one time payments to Baxter as follows:

(a) $2.0 million U.S. dollars between December 6 and December 31, 1992,

(b)$2.0 million U.S. dollars between December 6 and December 31, 1993,

(c) $2.0 million U.S. dollars between December 6 and December 31, 1994,

(d) $2.0 million U.S. dollars between December 6 and December 31, 2001.

> Maruishi shall determine in its sole discretion the actual date of payment, provided such date shall be within the periods set forth above.
>
> If the Abbott Agreement becomes effective but is then terminated prior to any of the above payment due dates, then any of these Section 3.1 payments due subsequent to termination shall no longer be due to Baxter from Maruishi, except that payment (a) shall be due even if the Abbott Agreement is terminated prior to December 31, 1992.
>
> 3.2 In addition to the Section 3.1 payments, Maruishi shall make royalty payments to Baxter based on the total quantity of Sevoflurane and HFIP sold to Abbott by Maruishi and also based on Abbott's Average Selling Price of Sevoflurane in the Territory. The royalty will be calculated using the following method and factors . . .

There followed a complicated methodology for determining the royalty payments due pursuant to the Baxter/Maruishi Agreement. The Baxter/Maruishi Agreement contemplated other agreements including but not limited to the following:

> (a) Maruishi entered into a Sevoflurane Supply and License Agreement with Abbott dated September 4, 1992 (hereafter *"Maruishi/Abbott Agreement"*);
>
> (b) Maruishi and Central Glass entered into a Licence and Manufacture Agreement dated September 18, 1992 (hereafter the *"Central Glass/Maruishi Agreement"*).
>
> (c) Abbott entered a side letter agreement with Central Glass dated September 18, 1992 (hereafter the *"Abbott/ Central Glass Side Letter"*).

In broad terms, the arrangement between these parties was that Central Glass would manufacture sevoflurane and HFIP for exclusive sale to Maruishi for resale exclusively to Abbott. Abbott was thus the party with the ultimate

responsibility for the commercial marketing and distribution of sevoflurane in the territory covered by these agreements. For this purpose, the Maruishi/Abbott Agreement contained (clause 14.1) *"an exclusive, non transferable licence in the territory under the Intellectual Property Rights and the Improvements, to sell Sevoflurane. . . ."* The 'Intellectual Property Rights' and the 'Improvements' as detailed in section 1.13 and 1.14 included the *"Licensed Patents and any improvements thereon"* and the *"Know-How and any Improvements thereon"* granted by Baxter to Maruishi by Clause 2 of Baxter/Maruishi Agreement. A dispute Resolution Agreement was entered into on September 4, 1992. Baxter, therefore, was the licensor of the Licensed Patents, and Abbott the sublicensee with no direct contractual relationship except as signatories to the Dispute Resolution Agreement.

The Dispute Resolution Agreement between Abbott, Baxter, Maruishi and Central Glass contained a detailed provision relating to the resolution of any disputes arising from the Baxter/Maruishi Agreement, the Maruishi/Abbott Agreement, the Central Glass/Maruishi Agreement and the Abbott/Central Glass Side Letter (hereafter singularly as *"Sevoflurane Agreement"* and collectively the *"Sevoflurane Agreements").*

Article 1 of the Dispute Resolution Agreement provided as follows:

> "1. *Purpose of Negotiation, Mediation and Arbitration.* It is the intent of the parties in entering into the Agreement that the provisions hereof be applied in such a way as to maintain to the extent reasonable the Commercialization of Sevoflurane and, at the same time, to maintain, to the extent reasonable, taking into consideration the nature of a breach by a party to a Sevoflurane Agreement and the impact thereof on the Original Commercial Relationship. The parties hereby

agree that, during the course of any negotiations, mediation or arbitration conducted pursuant to this Agreement or any of the Sevoflurane Agreements, they shall seek to achieve these goals and the parties hereby instruct all negotiators, mediators, any arbitrators under any of the Arbitration Clauses and any CPR Arbitration Panel (as defined below) to conduct such negotiations, mediation or arbitration, with the sole purpose of maintaining to the extent reasonable the Commercialization of Sevoflurane and at the same time returning, to the extent reasonable, taking into consideration the nature of a breach by a party to a Sevoflurane Agreement and the impact thereof on the Original Commercial Relationship, the relationship of the parties in an overall contractual and overall economic sense to the Original Commercial Relationship. Any negotiators, mediators and CPR Arbitration Panels shall resolve disputes submitted to negotiation, mediation or arbitration hereunder by the exercise of sound and impartial business judgment . . .

An 'Impairment of the Original Commercial relationship' shall mean: (a) an alleged breach or termination of one of the Sevoflurane Agreements that result or could reasonably be expected to result in any change or potential change in the Original Commercial Relationship that would: (i) cause a party to pay more to exercise any of its rights under any of the Sevoflurane Agreement than, but for such change, it would otherwise have been required to pay, including, without limitation, the purchase price such party is required to pay for Sevoflurane and/or HFIP; (ii) prevent a party from exercising any of the rights licensed or sublicensed to it under any of the Sevoflurane Agreements or performing any of its obligations undertaken under any of the Sevoflurane Agreements; (iii) reduce the amount a party would but for such change otherwise receive under any

> Sevoflurane Agreement; (iv) prevent a party from receiving its full rights or full commercial benefits under any of the Sevoflurane Agreements; (v) prevent or impair the commercialization of Sevoflurane; or (vi) otherwise impair the Original Commercial Relationship in such a way that it could be reasonably concluded that any one of the parties would not have entered into the Sevoflurane Agreements on the original terms and conditions actually set forth in the Sevoflurane Agreements if such change were in effect at the time of entering into the Sevoflurane Agreements, ...

Abbott obtained FDA approval for sevoflurane in 1995 and it became an immediate success in the United States, just as it had been in Japan. In 2000 alone, Abbott sold well over $100 million in sevoflurane in the United States. It's 2000 sevoflurane sales accounted for around 57.7 percent of the dollar sales of all the inhaled anesthetics sold by all United States' sellers during that year.

In 1998, Baxter acquired the Pharmaceutical Products Division of the Ohmeda health care business of The BOC Group. Ohmeda was Abbott's principal competitor in the sale of inhaled anesthetics in the U.S. Ohmeda had developed a method for making sevoflurane that did not infringe any of the Baxter patents previously assigned. This method of production, known as the three-step process, is the subject of U.S. Patent No. 5,886,239 (hereafter '239 Patent) dated March 23, 1999. Baxter is now the present owner of the '239 Patent.

Baxter decided to proceed with Ohmeda's plan to introduce a generic sevoflurane in the United States using the three-step process. Under the Hatch-Waxman Act, Abbott had a period of data exclusivity during which no one else could obtain FDA approval to sell sevoflurane relying upon the safety and efficacy data submitted by Abbott. The period ended in 2000, and Baxter filed an Abbreviated New Drug Application

(ANDA). Abbott sued Baxter for patent infringement, based upon the ANDA filing, in the following two cases, *Abbott Laboratories v. Baxter Pharmaceutical Products, Inc.*, No. 00-C-5939, and *Abbott Laboratories v. Baxter Pharmaceutical Products, Inc.*, No. 01-C-1867.

After Abbott learned of Baxter's plans to introduce a generic sevoflurane, Abbott claimed that if Baxter sold generic sevoflurane before the expiration of the sublicense agreement (December 2005), Baxter would violate the licensing agreement between Baxter and Maruishi, as well as the dispute resolution agreement between Baxter, Abbott, Maruishi, and Central Glass. Pursuant to the Dispute Resolution Agreement, Abbott demanded binding arbitration of its claim on May 25, 2000. The arbitration proceeding was convened in Chicago before a three member panel of arbitrators. The panel consisted of a U.S. attorney, a Spanish attorney, and a Japanese law professor. Neither Maruishi nor Central Glass participated in the proceedings before the arbitrators. The "Final Award" was entered June 15, 2001.

The panel determined that this language with "rights to sublicense" contained in the original Baxter/Maruishi Agreement granted Maruishi all rights to the Licensed Patents, along with rights to any "improvements" on the Licensed Patents. Baxter also granted Maruishi an exclusive license to the Know-How to make and use Sevoflurane and HFIP, with the right to sublicense. Know-How, as defined by the agreement, was tied to the Licensed Patents and the technology disclosed therein. The arbitrators recognized that the Licensed Patents all relate to the "one-step" process for manufacturing Sevoflurane and the three-step process which Baxter sought to market was not an infringement or an improvement on the one-step process. The facts presented at the hearing revealed that Ohmeda developed the three-step process independently from the one-step process through the use of information related to Baxter's expired patents, which were not part of the

Licensed Technology in the Baxter/Maruishi agreement. Thus, the three-step process did not use any of the Know-How from the one-step process.

The panel determined that Abbott is a third party beneficiary of the Baxter/Maruishi agreement and, therefore, had a right to sue. Pursuant to the Baxter/Maruishi agreement, Abbott has the express right to invoke the Dispute Resolution Agreement if it "reasonably believes that a dispute threatens to result in an Impairment of the Original Commercial Relationship." Any dispute of the Sevoflurane Agreements that could result in the Impairment of the Original Relationship is all that the Dispute Resolution Agreement requires. The tribunal found that the Dispute Resolution Agreement created an independent obligation to prevent impairment of the Original Commercial Relationship which would result in a breach of the Parties' obligations. Baxter admitted that should they re-enter the market with a generic sevoflurane, Abbott's sales of sevoflurane would be affected adversely, affecting the overall economic benefit for Abbott, Maruishi, and Central Glass. Therefore Baxter's sales of a generic sevoflurane would constitute an Impairment of the Original Commercial Relationship. As defined by clause (a)(iii), generic sales will "reduce the amount a party would but for such change otherwise receive under any Sevoflurane Agreement," constituting an impairment. The tribunal determined that on this basis, Baxter should be enjoined from selling a generic sevoflurane product through the term of the Baxter/Maruishi Agreement, which expires in June 2005, as to maintain the Original Commercial Relationship.

The arbitrators further found that the obligation of good faith under Illinois law establishes an independent cause of action under the Baxter/Maruishi Agreement. Although the Agreements are silent as to the issue of competition by Baxter, the arbitrators concluded it would be a breach of the duty of good faith for Baxter to "deprive its own sublicensee

of the fruits of its contract." Baxter's proposal to enter into the sevoflurane market will not only "hurt Abbott, but will also reduce Baxter's only royalties from Abbott's sales."

Baxter argued that any agreement between Baxter and Abbott that prevented Baxter from entering into the sevoflurane market would have anticompetitive implications and, therefore, would be illegal under United States antitrust law. The tribunal found that competitive implications were foreseeable by the Parties in 1992 when generic competition was expected after December 2000. The tribunal determined that Baxter had not established that competition is not still possible. It was Baxter's acquisition of Ohmeda and the '239 Patent, not the Sevoflurane Agreements, which removed Ohmeda from the sevoflurane market as an independent generic competitor with Abbott. Baxter has moved for summary judgment to vacate the arbitration award dated June 15, 2001.

JURISDICTION

This action arises under the federal antitrust laws, as well as under the Federal Arbitration Act and Chapter 2 thereof, 9 U.S.C. §§ 201-208, which implements the Convention of the Recognition and Enforcement of Foreign Arbitral Awards. This Court has subject-matter jurisdiction pursuant to 28 U.S.C. § 1331, 9 U.S.C. § 203, and 15 U.S.C. § 26. Venue is proper in this district based upon 28 U.S.C. § 1391(b), 9 U.S.C. § 204, and 15 U.S.C. § 22.

STANDARD OF REVIEW

Under the Convention, the district court's role in reviewing an arbitral award is strictly limited: "The court shall confirm the award unless it finds one of the grounds for refusal or deferral of recognition or enforcement of the award specified in the said Convention." 9 U.S.C. § 207. The grounds for refusing to recognize or enforce an arbitral award are set forth in section V of the Convention. Art. V(1)(2). The only ground

relevant for purposes of the parties' cross motions for summary judgment is if "cognition or enforcement of the award would be contrary to the public policy" of the country in which enforcement or recognition is sought.' Convention Art. V(2). Although the Seventh Circuit has stated that the Convention "contemplates the possibility of the award being set aside in a proceeding under local law," *Lander Co. v. MMP Invs., Inc.*, 107 F.3d 476, 481 (7th Cir.1997), *cert. denied,* 522 U.S. 811, 118 S.Ct. 55, 139 L.Ed.2d 19 (1997), thus we entertain Baxter's last two argunments. "Judicial review of an arbitration award is extremely limited." *E.I. DuPont de Nemours v. Grasselli Employees Independent Ass'n*, 790 F.2d 611, 614 (7th Cir.) *cert. denied* __ U.S. __, 107 S.Ct. 186, 92 L.Ed.2d 120 (1986). Baxter seeks vacation of the award pursuant to the contrary to public policy ground set forth in Art. V(2). We review Baxter's arguments keeping in mind that the arbitrators' findings are entitled to great deference by the court.

DISCUSSION

In support of its motion to vacate the arbitration award Baxter raises three substantive arguments.[1] First, Baxter contends that the arbitrators' interpretation of the sevoflurane contracts and the resulting award in Abbott's favor creates an illegal "market allocation" agreement in violation of section 1 of the Sherman Act. Next, Baxter contends that the award requires Abbott to violate a FTC consent decree. Finally, Baxter argues the award contravenes Illinois public policy

[1] In Baxter's motion to vacate Baxter also objects to the foreign arbitrators. We agree with Abbott that Baxter's argument as to the foreign arbitrators is untimely and thus constitutes a waiver precluding judicial review. *Health Serv. Mgmt. Corp. v. Hughes*, 975 F.2d 1253, 1263-64 (7th Cir.1992). Furthermore, the composition of the panel was dictated by the parties' agreement.

against enforcing unwritten covenants not to compete. Baxter admits that it presented these same arguments during the arbitration hearing.

1. Market Allocation In Violation of the Sherman Act.

Baxter argues that the tribunal's interpretation of the Sevoflurane Agreements is a market allocation agreement and thus is a *per se* violation of section 1 of the Sherman Act. Baxter claims that the market allocation agreement here-if enforced-will eliminate domestic competition in the sale of sevoflurane in the short run and delay the onset of generic competition through a comprehensive allocation of the United States market for the sale of sevoflurane. The agreement allegedly will cost U.S. sevoflurane purchasers between $200 and $300 million as a result of the higher prices that Abbott will be able to charge in the absence of competition.

In support of this argument Baxter offers two affidavits, of its employees Ronald Quadrel and Raul A. Trillo, Jr. These affidavits were not submitted to the arbitrators. We find that Baxter's tardy submission of these affidavits is improper and strike these affidavits with prejudice. Baxter offers no justification for its failure to present this evidence by way of testimony during the arbitration hearing.

Under § 1 of the Sherman Act, 15 U.S.C. § 1, "[e]very contract, combination . . . , or conspiracy, in restraint of trade" is illegal. "Although the Sherman Act, by its terms, prohibits every agreement 'in restraint of trade,' [the Supreme] Court has long recognized that Congress intended to outlaw only unreasonable restraints." *State Oil Co. v. Khan*, 522 U.S. 3, 7, 118 S.Ct. 275, 139 L.Ed.2d 199 (1977). There are two separate types of section 1 violations. If the rule of reason applies, plaintiff must prove that defendants' actions resulted in an unreasonable restraint of trade. Alternatively, plaintiff must prove that defendants' conduct falls within one of several categories that are conclusively

presumed to be illegal *per se* violations of section 1. If plaintiff proves that defendants' conduct falls within one of these categories, it is not necessary to prove that the conduct resulted in an unreasonable restraint on trade. *See Arizona v. Maricopa County Medical Soc'y*, 457 U.S. 332, 343-48, 102 S.Ct. 2466, 2472-75, 73 L.Ed.2d 48 (1982).

When analyzing a motion for summary judgment on a section 1 claim, the Supreme Court has held that "antitrust law limits the range of permissible inferences from ambiguous evidence in a § 1 case." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U .S. 574, 588, 106 S.Ct. 1348, 1356, 89 L.Ed.2d 538 (1986). For section 1 claims the nonmovant must submit more than ambiguous evidence of the alleged conspiracy to withstand a motion for summary judgment. "Conduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy." *Id.*

Baxter, deferring to the findings of the two foreign arbitrators, claims that the Baxter/Maruishi Agreement contains "an implied market allocation" and the arbitration award forbids Baxter from selling sevoflurane in competition with Abbott until December 10, 2005. A review of the award offers little support for Baxter's *per se* violation theory.

A *market* allocation agreement is an "agreement between competitors at the same level of market structure to allocate territories in order to minimize competition[.]" *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 608, 92 S.Ct. 1126, 31 L.Ed.2d 515 (1972). *Per se* rules apply only to agreements which "always or almost always tend to restrict competition." *Broadcast Music, Inc. v. Columbia Broad. Systems, Inc.*, 441 U.S. 1, 19-20, 99 S.Ct. 1551, 60 L.Ed.2d 1 (1979). However, the Supreme Court has been reluctant to "extend *per se* analysis to restraints imposed in the context of business relationships where the economic impact of certain practices

is not immediately obvious." *Federal Trade Comm'n v. Indiana Fed'n of Dentists*, 476 U.S. 447, 458-59, 106 S.Ct. 2009, 90 L.Ed.2d 445 (1986).

The tribunal accepted Abbott's argument on this issue. The arbitrators specifically found the following:

> Baxter's evidence assumed that the Sevoflurane Agreements obligated Baxter to license the three-step process to Abbott, whereas this Tribunal considers that the three-step process is not included in the license granted to Maruishi and sublicensed to Abbott under the Sevoflurane Agreements (see §§ 19-22 above). This is not a case of the Sevoflurane Agreements having any competitive implications that were not foreseeable by the Parties in 1992 when generic competition was expected after December 2000, and Baxter has not established that such competition is not still possible. The apparent antitrust issues relating to the Sevoflurane market that Baxter now seeks to rely upon to escape its contractual obligations under the Sevoflurane Agreements do not arise from those Agreements themselves, but as a result of Baxter's acquisition of Ohmeda and the 239 Patent, which removed from the Sevoflurane market the very type of independent generic competitor foreseen by the Parties in 1992.

Pages 18-19 ¶¶ 34-35.

We agree with the arbitrators on this very important point. In addition, as Abbott asserts, the present arrangement is such that the "competitive effect can only be evaluated by analyzing the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed," known as the rule of reason analysis. *Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 692 98 S.Ct. 1355, 55 L.Ed.2d 637 (1978). The contractual arrangement with Abbott and Baxter and Baxter's subsequent acquisition of Ohmeda creates a

unique situation in light of the terms of the original commercial relationship language in the agreements. Furthermore, the injury now alleged by Baxter is not your typical type of antitrust injury. Here, Baxter who profits tremendously from its contractual arrangement with Abbott, wants to increase its profits by introducing generic sevoflurane, thus establishing its presence in the generic submarket as well as the existing sevoflurane market which Baxter currently profits from.

Baxter fails to cite to any case law where the *per se* analysis has been applied to void a licensing agreement thereby allowing a licensor to compete with its sublicensee in the product market that is the subject of the license agreement. Rather, Baxter cites to *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 608, 92 S.Ct. 1126, 31 L.Ed.2d 515 (1972) in which the Supreme Court found an agreement between an association of independent grocers to be a geographical market allocation and thus a *per se* Sherman Act violation. 405 U.S. at 600. Moreover, there is no evidence in the record as to the parties' intent to divide the market or minimize competition. We find the present arrangement differs from *Topco* in that Baxter has not alleged that the agreements are "naked restraints on trade with no purpose except stifling of competition." *Id.* at 608 (quoting *White Motor Co. v. United States*, 372 U.S. 253, 263, 83 S.Ct. 696, 9 L.Ed.2d 738 (1963)). The record is silent with respect to Abbott's harm to generic competition. Baxter has also failed to allege that another generic producer could not compete with Abbott in the sale of sevoflurane. In fact, Ohmeda was free to compete with Abbott in the sevoflurane market prior to its acquisition by Baxter. Thus, the only adverse impact on competition was due to the actions of Baxter and not the tribunal's interpretation of the Sevoflurane Agreements.

Baxter also cites to *Blackburn v. Sweeney*, in which the Seventh Circuit held that an agreement between two former law partners to allocate advertising to specific territories in

Indiana was an agreement to allocate markets and thus the *per se* rule should apply. 53 F.3d 825, 827 (7th Cir.1995). In *Blackburn*, the court determined that the agreement not to compete "was not a necessary condition for the increased competition resulting from the split-up of the partnership: . . . the partnership was essentially over at the time the Agreement was entered." *Id.* at 828. In fact, the evidence presented to the arbitrators reveals that during the 1980's Baxter decided to license the rights to market sevoflurane, rather than market it directly. There were no facts presented to the arbitrators to support any type of market allocation. Rather, Baxter decided not to manufacture and market sevoflurane because it did not have the capacity to do so. Anyone else in the position to sell a generic sevoflurane will be able to do so once this other competitor's ANDA is approved by the FDA. Furthermore, the agreement granting Abbott a sublicense of the Baxter technology will expire in December 2005, and Baxter will then be free to compete.

In the alternative, Baxter argues that, even if, the arbitrators' decision prohibiting Baxter from selling generic sevoflurane is not concluded to be an illegal market allocation under the Sherman Act it must be viewed as an "ancillary covenant not to compete." Relying on *Compton v. Metal Prods., Inc.*, 453 F.2d 38 (4th Cir.1971), Baxter contends that an ancillary covenant not to compete is also an unreasonable restraint on trade under the antitrust laws. We again find the law relied on by Baxter to be factually distinct from the case at bar. Paragraph 15 of the license agreement in *Compton* stated that Compton would not "engage in any business or activity relating to the manufacture or sale of equipment of the type licensed hereunder. . . ." *Compton*, 453 F.2d at 44. Thus, the licensor agreed not to sell any coal mining screw conveyors, whether or not covered by the patent. The court in *Compton*, stated that Paragraph 15 did not appear to be an ancillary agreement, given that the licensor agreed to remove itself completely from the mining machine manufacturing

business. *Id.* at 45. Obviously, the *Compton* agreement is much broader than the sevoflurane agreements, in which Baxter is free to sell other inhaled anesthetics, and in fact admits to the sale of the competing products desflurane and isoflurane.

Baxter relying on *Palmer v. BRG of Georgia, Inc.*, 498 U.S. 46, 111 S.Ct. 401, 112 L.Ed.2d 349 (1990) also argues that the arbitrators limited the restriction to the United States rather than splitting up the market between Abbott and Baxter. In *Palmer*, the Supreme Court held that an agreement between two bar review course providers, who agreed not to compete against each other, assigning one provider to the entirety of Georgia, was *per se* unlawful. *Id.* at 47. The *Palmer* court concluded that the agreement between the parties was a naked restraint because it was formed for the purpose of raising the price of the product in question. *Id.* at 47-49. Here, there is no allegation that the agreement between Abbott and Baxter was created to raise the price of sevoflurane. In fact, Baxter was never a competitor with Abbott in the sevoflurane market, whereas in *Palmer,* the two parties were actual *competitors* that agreed to not compete. *See Palmer,* 498 U.S. 46. The arbitrators were presented with the undisputed facts that Baxter exclusively licensed its ability to commercialize the licensed patents in the United States to Abbott; the licensing agreements created a new competitor to existing inhaled aesthetics, whereas the competitor in *BRG* was plainly eliminated due to their agreement. And once again, competition in the sevoflurane market is still possible not just from Baxter.

Moreover, to satisfy as a reasonable ancillary restraint, an agreement must be "ancillary to the main business purpose of a lawful contract" and "necessary to protect the covenantee's legitimate property interests, which require that the covenants be as limited as is reasonable to protect the covenantee's interests." *Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255,

265 (7th Cir.1981). Baxter contends that the agreements are not "ancillary" to the "main business purpose." However the two cases Baxter cites for this contention, *Palmer* and *Compton*, contain agreements which are distinguishable from the sevoflurane agreements in this case. In *Palmer*, the agreement was entered into for the purpose of raising prices in the specified market. *See Palmer*, 498 U.S. at 47. There is no such agreement here. In *Compton*, the agreement in effect removed Compton from the mining machine business entirely, which is not the case here, as Baxter is free to sell other inhaled anesthetics and admits to doing so. *See Compton*, 453 F.2d at 45. As the arbitral panel found, Abbott has never argued or attempted to preclude generic competition generally in sevoflurane; the only competitor that Abbott has sought to prohibit for selling a generic sevoflurane is its own exclusive licensor, Baxter. (R.237). In fact, as the arbitrators concluded, if Baxter had not acquired the Ohmeda assets, then Ohmeda may have been competing with Abbott in the sale of sevoflurane today. *Id.* Moreover, the arbitration does not affect Baxter's right to sell its desflurane and isoflurane products in competition with Abbott's sevoflurane or the sales or other anesthetic products by other competitors. Baxter has not established that generic competition is not still possible.

Baxter also contends that the Agreements are too broad, extending to any sevoflurane product and not just the patented technology, thereby not satisfying the second requirement. However, Baxter fails to recognize that this court must ask "whether an agreement promoted enterprise and productivity at the time it was adopted." *See Polk Bros. v. Forest City Enterprises*, 776 F.2d 185, 189 (7th Cir.1985). Here, Baxter admits that the agreements promoted the enterprise because Abbott sold over $100 million in sevoflurane in the U.S. in 2000, accounting for 57.7 percent of the dollar sales of all the inhaled anesthetics sold by all U.S. sellers during that year. It is also evident that Abbott

expended a significant amount of money, approximately $1.4 billion, into the commercial development of sevoflurane. These property interests must be protected and Baxter admits that its entry into the market would reduce Abbott's profits as well as Baxter's royalties. The arbitrators rejected this precise argument on the very logical ground that the antitrust issues raised by Baxter "do not arise from those [Sevoflurane] Agreements themselves, but as a result of Baxter's acquisition of Ohmeda and the 239 Patent, which removed from the sevoflurane market the very type of independent generic competitor foreseen by the Parties in 199 [sic]." (R. 3267). Finally, there is no evidence in the record that Abbott sought to harm generic competition whatsoever. As Abbott points out the only circumstance in which the award could even conceivably could affect competition is if Baxter retains control of the Ohmeda three-step process and does not transfer this process to another manufacturer.

The evidence presented to the arbitrators fails to state a section 1 claim under a rule of reasonable analysis The rule of reason analysis is applicable to "agreements whose competitive effect can only be evaluated by analyzing the facts peculiar to the business involved, the particular restraint's histoy and the reasons it was imposed." *Wilk v. American Med. Ass'n*, 895 F.2d 352, 358 (7th Cir.1990). The United States Department of Justice and Federal Trade Commission Antitrust Guidelines for the Licensing of Intellectual Property (1995) ("Intellectual Property Guidelines") recognize that in general "restraints in intellectual property licensing arrangements are evaluated under the rule of reason." Intellectual Property Guidelines, § 3.4. In applying the rule of reason, "the fact finder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing a unreasonable restraint on competition." *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 97 S.Ct. 2549, 53 L.Ed.2d 568 (1977). Baxter argues that even if the rule of reason analysis is applied that the agreements would

still be unlawful because of its anticompetitive effects, relying on the current market share of sevoflurane to show the anticompetitive effects of the agreement. However, as Abbott points out, these effects should be judged at the time the contract was entered in not after its objectives have been accomplished. *See Polk Bros.*, 776 F.2d at 189. In this case, at the time the agreements were entered into, sevoflurane was not even on the market. Therefore, the licensing arrangement was pro-competitive, in that it promoted Abbott's investment to introduce the product into the United States and Baxter cannot artificially create antitrust claims by narrowly defining the relevant market to be only Abbott and Baxter. In addition, any anticompetitive consequence is a product of the parties agreements. Other competitors are free to enter the market.

2. The Award Does Not Require Abbott to violate a FTC Consent Decree

Baxter's second argument alleges that the final award requires Abbott to violate a FTC Consent Decree. This court agrees with Abbott that Baxter does not have standing to enforce the FTC Decree. In *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 750, 95 S.Ct. 1917, 44 L.Ed.2d 539 (1975), the Supreme Court reiterated the well-settled rule that "a consent decrees is not enforceable directly or in collateral proceedings by those who are not parties to it, even though they were intended to be benefitted by it." *Id.* at 750, 95 S.Ct. 1917. "Cases involving antitrust consent decrees have hewed closely to the *Blue Chip* rule barring any person not directly participating in the consent decree from suing to enforce its terms." *Coca-Cola Bottling Co. of Elizabethtown, Inc. v. Coca-Cola Co.*, 654 F. Supp 1419, 1437 (D.De.1987), *aff'd*, 988 F.2d 386 (3rd Cir.), *cert. denied*, 510 U.S. 908, 114 S.Ct. 289, 126 L. Ed2d 239 (1993). Indeed, Baxter has not cited a single case in which a nonparty to a government antitrust consent decree was permitted to enforce the decree.

Moreover, Baxter contends that the Award causes Abbott to violate paragraphs III and II(B) the consent decree. Paragraph III provides in part that where Abbott is a party to an infringement action in which it is the New Drug Application ("NDA") holder, it cannot be a party to an agreement with the alleged infringer by which the parties agree not to dismiss the litigation, the NDA holder provides compensation to the alleged infringer and the alleged infringer agrees to refrain from selling drug containing the product at issue. This provision does not apply, however, because at the time of the Sevoflurane Agreements, Baxter was the owner of the patents and not the alleged infringer. Secondly, there was no pending litigation between Abbott and Baxter relating to sevoflurane at the time of the Agreements. There has also been no agreement to not dismiss the litigation, nor has there been an agreement that Baxter would be paid to not sell a product until the litigation was resolved. Thus paragraph III does not apply.

Paragraph II(B) provides that Abbott may not be a party to an agreement in which it is an ND holder and another party is the Abbreviated New Drug Application ("ANDA") first filer, pursuant to which the ANDA first filer agrees to refrain from researching, developing, manufacturing, marketing or selling a drug product that is not the subject of a patent infringement action. This paragraph also does not apply to the Sevoflurane Agreements given that the Agreements were not made between an NDA holder and an ANDA first filer. Baxter was the patent owner and had not filed an ANDA for sevoflurane. The fact that Baxter is now an ANDA filer is only a consequence of its acquisition of Ohmeda as the panel recognized. Baxter's actions cannot change the terms of the Agreement. Thus paragraph II(B) is also inapplicable. For all these reasons, this court finds that Baxter does not have standing to enforce the FTC Decree.

3. The Arbitration Award does not Contravene Illinois' public policy.

Baxter's final argument contends that the Arbitration Award creates an implied covenant not compete, which is contrary to Illinois public policy. While a court is reluctant to do so, it may vacate an award for violating a public policy that is "explicit," "well-defined," and "dominant" as "ascertained by reference to the laws and legal precedents and not from general considerations of proposed public interest." *United Paperworkers Int'l Union v. Misco, Inc.* 484 U.S. 29, 42, 108 S. Ct 364, 98 L. Ed2d 286 (1987). Baxter cites 740 ILCS 10/3 (2001), which states that agreements between a person and "any other person who is, or but for a prior agreement would be a competitor" which act to divide "customers, territories, supplies, sales, or markets, functional or geographical, for any commodity or service," are forbidden. However, this statute does not specifically address implied covenants not to compete, but rather is a general antitrust statute. "[R]estrictive covenants in employment contracts are looked at with more scrutiny than such covenants that are ancillary to the sale of a business. . . ." *Eichmann v. Natn'l Hosp. and Health Care Servs., Inc.*, 308 Ill.App.3d 337, 344 (1st Dist.1999). According to Abbott's submissions no Illinois statute prohibits implied covenants not to compete. In the present case, the implied covenant not to compete is coterminous with the existing licensing agreement and Abbott does not seek protection after the expiration of the license agreement on December 10, 2005. "In order for a noncompetition agreement to be valid, [ ] it must be ancillary to a valid transaction, such that the covenant not to compete is subordinate to the main purpose of the transaction." *Liautaud v. Liautaud*, 221 F.3d 981, 986 (7th Cir.2000). Thus, the "covenant" is ancillary to the valid Sevoflurane Agreements, which were established for the main purpose of commercially developing sevoflurane.

Baxter further argues that the covenant is not reasonable and Illinois courts have refused to "modify a restrictive covenant" to make it reasonable where modifying the covenant "would be tantamount to fashioning a new agreement." *See Eichmann*, 308 Ill.App.3d at 347. However, in this case, the scope of the covenant not to compete is also reasonable by definition. The reasonableness of the restraint depends on the "time and territory as judged by the circumstances of the particular case." *Sheehy v. Sheehy*, 299 Ill.App.3d 996, 1004 (2nd Dist.1998). Here, the scope is no greater than that of the Sevoflurane Agreements and is, therefore, reasonable. After reviewing the record it can only be concluded that the arbitrators obviously considered and rejected the defenses now urged by Baxter as grounds to vacate the Award.

CONCLUSION

For the foregoing reasons Abbott's motion to confirm the Arbitration Award is hereby granted. Baxter's motion to vacate is denied with prejudice. Both cases are hereby terminated and all other pending motions terminated as moot. This is a final and appealable order.

So Ordered.

APPENDIX C

ABBOTT LABORATORIES

v.

BAXTER INTERNATIONAL INC

FINAL AWARD

I. *AWARD*

§1.- This is the final award in an arbitration between the Parties pursuant to the Dispute Resolution Agreement (see §3 below).

II. *PARTIES*

§2.- The Claimant is ABBOTT LABORATORIES, an Illinois Corporation, having its principal place of business at One Abbott Park Road, Abbott Park, Illinois 60064-3500, United States of America, (hereafter, "*Abbott*" or "*Claimant*"), represented in this arbitration by Mr. R. Mark McCareins and Ms. Marie A. Lona of Winston & Strawn, Chicago, Illinois.

The Respondent is BAXTER INTERNATIONAL INC., a Delaware Corporation with its principal offices at One Baxter Parkway, Deerfield, Illinois 60015, United States of America (hereafter "*Baxter*" or "*Respondent*"), represented in this arbitration by Mr. David T. Pritikin and Mr. Marc E. Raven of Sidley & Austin, Chicago, Illinois.

The Claimant and the Respondent are hereafter jointly referred to as the "*Parties*".

III. *REFERENCE TO ARBITRATION*

§3.- This arbitration arises pursuant to a Dispute Resolution Agreement dated September 18, 1992 (hereafter "*the Dispute Resolution Agreement*"), executed by four parties: Abbott, Baxter, and two Japanese Corporations called Central Glass Co, Ltd and Maruishi Pharmaceutical Co. Ltd (hereafter "*Central Glass*" and "*Maruishi*" respectively).

The Dispute Resolution Agreement provided a procedure for the resolution of any disputes that might arise between Abbott, Baxter, Central Glass and Maruishi under various agreements relating to the commercial development of an inhalation anaesthetic known as Sevoflurane. Article 7.1 of the Dispute Resolution Agreement entitled '*Arbitration*' provided as follows:

"*7. Arbitration*

7.1 Submission of Dispute to Arbitration.

Any matter that has been submitted to arbitration . . . shall be settled by arbitration in accordance with the Center for Public Resources Rules for Non-Administered Arbitration of International Disputes (the 'CPR Rules') by three arbitrators (the 'CPR Arbitral Panel') who shall be appointed by the Center for Public Resources from its Panels of Distinguished Neutrals in accordance with Rule 6 of the CPR Rules. One such arbitrator shall be a Japanese national fluent in the English language, one shall be a U.S. national, and the third shall be a person fluent in English and a national of a country other than Japan or the U.S. In resolving a dispute, the CPR Arbitral Panel shall apply the substantive law, if any, set forth in the Sevoflurane Agreement under which such dispute arose as the governing law of such Sevoflurane Agreement and, if none is specified, the CPR Arbitral Panel shall apply the substantive law of Japan or the State of Illinois, whichever the CPR Arbitral Panel determines appropriate. The arbitration

shall be conducted in the English language . . . and shall be held at a neutral site designated by the CPR Arbitral Panel . . ."

Pursuant to Article 7.1 an Arbitral Tribunal was appointed by the Centre for Public Resources and this arbitration has been conducted pursuant to the Centre for Public Resources '*Rules for Non-Administered Arbitration of International Disputes*' as revised and effective from September 15, 2000.

IV. *THE ARBITRAL TRIBUNAL*

§4.- The members of the Arbitral Tribunal appointed pursuant to Article 7.1 are Mr. Gaynell Methvin of Dallas, Texas, U.S.A., Professor Kazuo Iwasaki of Inuyama City, Japan, and Dr. Bernardo M. Cremades of Madrid, Spain.

V. *THE SEVOFLURANE AGREEMENTS*

§5.- Sevoflurane is an inhalation anaesthetic first developed by Baxter scientists in the mid-1960s and since then has been subject to a product patent and various process patents in the United States and elsewhere.

Baxter succeeded in developing an efficient process for the production of Sevoflurane in which a chemical called HFIP is mixed with formaldehyde and hydrogen fluoride in the presence of sulphuric acid and heat. This process was referred to during the arbitration as the "*one-step process*" in order to distinguish it from the "*three-step process*" developed by a company called Ohmeda (see §12 below).

The one-step process was or is the subject of various US patents owned by Baxter (particular Patents No. 4,250,334 and 4,469,898, (hereafter the "*334 and 898 Patents*") and counterpart patents in other countries. The three-step process is the subject of U.S. Patent No. 5,886,239 (hereafter "*239 Patent*") dated March 23, 1999 and presently also owned by Baxter.

§6.- During the 1980's Baxter decided to licence the rights to market Sevoflurane, rather than market it directly. It developed a relationship with Maruishi who commercially developed Sevoflurane with great success in Japan. There were various agreements between Baxter and Maruishi, but the important agreement for the purposes of this arbitration is a Patent and Know-How Licence Agreement dated September 3, 1992 (hereafter "*Baxter/Maruishi Agreement*").

Clause 2.1 of the Baxter/Maruishi Agreement granted licences in the following terms:

> "*2.1. Baxter hereby grants to Maruishi an exclusive license even as to Baxter under the Licensed Patents and any improvements thereon to make, use, have made, sell, and have sold Sevoflurane and HFIP throughout the 'Territory', with rights to sublicense. The 'Territory' shall mean the world, excluding Japan, North and South Korea, and the People's Republic of China exclusive of Hong Kong. 'Sevoflurane and HFIP' shall mean Sevoflurane and HFIP manufactured using a process that but for the license granted therein would infringe one or more of the Licensed Patents.*
>
> *2.2 Baxter hereby grants to Maruishi an exclusive license even as to Baxter under the Japanese Patents and any improvements thereon to make Sevoflurane and HFIP in Japan, and to sublicense Central Glass to make Sevoflurane and HFIP in Japan, for sale exclusively to Maruishi for resale by Maruishi in Japan exclusively to Abbott in Japan for resale by Abbott throughout the Territory.*"

Clause 1.2 defined 'Licensed Patents' as various patents relating to HFIP and/or Sevoflurane listed in Exhibit A to the Baxter/Maruishi Agreement. These included the 334 and 898 Patents, but not the 239 Patent.

§7.-The Baxter/Maruishi Agreement also contained a Know-How License in clause 2.3:

> "*2.3 Baxter hereby grants Maruishi an exclusive license even as to Baxter to use the Know-How and any improvements thereon to make, use, have made, sell and have sold Sevoflurane and HFIP in the Territory, with rights to sublicense, and an exclusive license even as to Baxter with rights to sublicense to Central Glass to use the Know-How and any improvements thereon to make and use Sevoflurane and HFIP in Japan for sale exclusively to Maruishi in Japan and resale by Maruishi exclusively to Abbott in Japan for resale by Abbott throughout the territory.*"

'Know-How' was defined in clause 1.1 as follows:

> "*1.1 Prior to January 1983, Baxter developed a new inhalant anaesthetic known as 'Sevoflurane' through the Phase I clinical trial stage in accordance with the guidelines of the United States Food and Drug Administration ('FDA') and, as a part of such development, acquired confidential proprietary information ('Know-How'). Baxter has supplied Maruishi with all Know-How relating to Sevoflurane and/or HFIP (an immediate form of Sevoflurane), including physico-chemical date, stability profiles, toxicity studies, mutagenicity studies, metabolic and pharmaco-kinetic data, and copies of all FDA correspondence, which have been collected by Baxter.*"

§8.- Section 3 of the Baxter/Maruishi Agreement provided for payments for the licence granted by Baxter:

> "*3.0 Payments*
>
> *3.1. For the Section 2 license grant, Maruishi shall make four (4) nonrefundable one time payments to Baxter as follows:*
>
> *(a) $2.0 million U.S. dollars between December 6 and December 31, 1992,*

(b) $2.0 million U.S. dollars between December 6 and December 31, 1993,

(c) $2.0 million U.S. dollars between December 6 and December 31, 1994,

(d) $2.0 million U.S. dollars between December 6 and December 31, 2001.

Maruishi shall determine in its sole discretion the actual date of payment, provided such date shall be within the periods set forth above.

If the Abbott Agreement becomes effective but is then terminated prior to any of the above payment due dates, then any of these Section 3.1 payments due subsequent to termination shall no longer be due to Baxter from Maruishi, except that payment (a) shall be due even if the Abbott Agreement is terminated prior to December 31, 1992.

3.2 In addition to the Section 3.1 payments, Maruishi shall make royalty payments to Baxter based on the total quantity of Sevoflurane and HFIP sold to Abbott by Maruishi and also based on Abbott's Average Selling Price of Sevoflurane in the Territory. The royalty will be calculated using the following method and factors . . .".

There followed a complicated methodology for determining the royalty payments due pursuant to the Baxter/Maruishi Agreement.

§9.- It is apparent from the references to Abbott and Central Glass in the Baxter/Maruishi Agreement that the Baxter/Maruishi Agreement contemplated further agreements including these two corporations. Accordingly,

(a) Maruishi entered into a Sevoflurane Supply and License Agreement with Abbott dated September 4, 1992 (hereafter "*Maruishi/Abbott Agreement*");

(b) Maruishi and Central Glass entered into a Licence and Manufacture Agreement dated September 18, 1992 (hereafter the "*Central Glass/Maruishi Agreement*");

(c) Abbott entered a side letter agreement with Central Glass dated September 18, 1992 (hereafter the "*Abbott/ Central Glass Side Letter*").

In broad terms, the arrangement between these parties was that Central Glass would manufacture Sevoflurane and HFIP for exclusive sale to Maruishi for resale exclusively to Abbott. Abbott was thus the party with the ultimate responsibility for the commercial marketing and distribution of Sevoflurane in the territory covered by these agreements. For this purpose, the Maruishi/Abbott Agreement contained (clause 14.1) "*an exclusive, non transferable licence in the Territory under the Intellectual Property Rights and the Improvements, to sell Sevoflurane . . .*". The 'Intellectual Property Rights' and the 'Improvements' as detailed in section 1.13 and 1.14 included the "*Licensed Patents and any improvements thereon*" and the "*Know-how and any improvements thereon*" granted by Baxter to Maruishi by Clause 2 of Baxter/Maruishi Agreement. Baxter therefore was the licensor of the Licensed Patents, and Abbott the sub-licensee with no direct contractual relationship except as signatories to the Dispute Resolution Agreement.

§10.- The Dispute Resolution Agreement between Abbott, Baxter, Maruishi and Central Glass contained detailed provisions relating to the resolution of any disputes arising from the Baxter/Maruishi Agreement, the Maruishi/Abbott Agreement, the Central Glass/Maruishi Agreement and the Abbott/Central Glass Side Letter (hereafter singularly as "*Sevoflurane Agreement*" and collectively the "*Sevoflurane Agreements*").

Article 1 of the Dispute Resolution Agreement provided as follows:

> "*1. Purpose of Negotiation. Mediation and Arbitration. It is the intent of the parties in entering into this Agreement that the provisions hereof be applied in such a way as to maintain to the extent reasonable the*

Commercialisation of Sevoflurane and, at the same time, to maintain, to the extent reasonable, taking into consideration the nature of a breach by a party to a Sevoflurane Agreement and the impact thereof on the Original Commercial Relationship, the Original Commercial Relationship. The parties hereby agree that, during the course of any negotiations, mediation or arbitration conducted pursuant to this Agreement or any of the Sevoflurane Agreements, they shall seek to achieve these goals and the parties hereby instruct all negotiators, mediators, any arbitrators under any of the Arbitration Clauses and any CPR Arbitration Panel (as defined below) to conduct such negotiations, mediation or arbitration, with the sole purpose of maintaining to the extent reasonable the Commercialisation of Sevoflurane and at the same time returning, to the extent reasonable, taking into consideration the nature of a breach by a party to a Sevoflurane Agreement and the impact thereof on the Original Commercial Relationship, the relationship of the parties in an overall contractual and overall economic sense to the Original Commercial Relationship. Any negotiators, mediators and CPR Arbitration Panels shall resolve disputes submitted to negotiation, mediation or arbitration hereunder by the exercise of sound and impartial business judgment . . .

An 'Impairment of the Original Commercial Relationship' shall mean: (a) an alleged breach or termination of one of the Sevoflurane Agreements that results or could reasonably be expected to result in any change or potential change in the Original Commercial Relationship that would: (i) cause a party to pay more to exercise any of its rights under any of the Sevoflurane Agreements than, but for such change, it would otherwise have been required to pay, including, without limitation, the purchase price such party is required to pay for Sevoflurane and/or HFIP; (ii) prevent a party from exercising any of the rights licensed or sublicensed

to it under any of the Sevoflurane Agreements or performing any of its obligations undertaken under any of the Sevoflurane Agreements; (iii) reduce the amount a party would but for such change otherwise receive under any Sevoflurane Agreement; (iv) prevent a party from receiving its full rights or full commercial benefits under any of the Sevoflurane Agreements; (v) prevent or impair the Commercialization of Sevoflurane, or (vi) otherwise impair the Original Commercial Relationship in such a way that it could be reasonably concluded that any one of the parties would not have entered into the Sevoflurane Agreements on the original terms and conditions actually set forth in the Sevoflurane Agreements if such change were in effect at the time of entering into the Sevoflurane Agreements, ... " (emphasis added).

VI. *APPLICABLE LAW*

§11.- Article 8.2 of the Dispute Resolution Agreement provides:

> "*8.2 Governing Law. The validity, interpretation, enforceability and performance of this Agreement shall be governed by and construed in accordance with the laws of the State of Illinois.*"

Article 7.1 of the Dispute Resolution Agreement also provides (see above §3) that the Tribunal "*shall apply the substantive law, if any, set forth in the Sevoflurane Agreement under which the dispute arose*". In this case the most important of the Sevoflurane Agreements is the Baxter/ Maruishi Agreement, in which Article 10.2 provides that "*The Law of the United States and the State of Illinois shall be applied including the provisions of the United States Arbitration Act 9 U.S.C. §1-16 to all disputes arising under this 1992 Licence Agreement.*"

Finally Rules 10.2 of the CPR Rules requires that the Arbitral Tribunal "*shall decide in accordance with the terms of the contract and shall take into account usages of the trade applicable to the contract.*"

VII. *CLAIMS AND DEFENCES OF THE PARTIES*

§12.- The commercial arrangements of the Sevoflurane Agreements proved highly successful. Abbott obtained Food and Drug Administration approval for Sevoflurane in 1995 and today it is the most widely used maintenance agent for general anaesthesia in the United States.

The successful introduction of Sevoflurane into the United States by Abbott encouraged a U.S. corporation called Ohmeda (then owned by the British Oxygen Company) to investigate the possibility of introducing a generic Sevoflurane in competition with Abbott, after a period of exclusivity granted to Abbott under Food and Drug Administration rules expired on December 7, 2000. In order to introduce a competing Sevoflurane product, however, Ohmeda had to discover a way to manufacture Sevoflurane economically without infringing Baxter's 334 and 898 Patents.

Ohmeda assigned a team of chemists to the project, and developed a new three-step process. On November 21, 1997 a patent application was filed on the novel third step of the three-step process and a U.S. patent—the 239 Patent—was issued on March 23, 1999. Meanwhile, on April 4, 1998, Baxter had acquired Ohmeda. Accordingly, the 239 Patent is now held by Baxter.

During 1998 Baxter decided to proceed with to introduce a generic Sevoflurane produced by the three-step process under the 239 Patent in competition with Abbott's sales of Sevoflurane pursuant to the Sevoflurane Agreements. On May 30, 2000 Abbott supplied Baxter with a 'Notice of Dispute' under the Dispute Resolution Agreement, this initiating this arbitration.

§13.- In its Pre-Hearing Memorandum dated February 2001, Abbott summarised its claims in this arbitration as follows:

"STATEMENT OF CLAIMS

1. *Abbott is a third-party beneficiary to the 1992 Baxter/ Maruishi License Agreement.*
2. *Baxter's entry into the Sevoflurane market will impair the 'Original Commercial Relationship' among the parties to the 1992 Sevoflurane Agreements.*
3. *The 1992 Baxter/Maruishi License Agreement obligates Baxter to convey all future advances in Sevoflurane to Maruishi, and therefore, to Abbott.*
   a. *Baxter has breached its express warranty to convey all Sevoflurane and HFIP-related intellectual property (patents and know-how) to Maruishi and, therefore, Abbott.*
   b. *Baxter's intention to market and sell Sevoflurane is an act of bad faith and impairs Abbott's rights to receive the fruits of its contracts.*
4. *Under equitable principles, Baxter is estopped from entering the Sevoflurane market.*
   a. *Baxter is legally estopped from entering the Sevoflurane market because such entry would violate its obligations under the 1992 Sevoflurane Agreements.*
   b. *Under the theory of promissory estoppel, Baxter cannot sell Sevoflurane during the contract term because of its repeated assurances that it would not do so.*
5. *Baxter's sale of Sevoflurane would constitute unfair competition by its misuse of confidential and competitive information."*

In the Pre-hearing Memorandum of Baxter International Inc dated February 16, 2001, Baxter summarised its defences under the following headings:

> "*I. The Technology License to Maruishi does not include the Three-Step Process and therefore the Three-Step is not encompassed within Abbott's sublicense*
>
> *A. The Ohmeda Three-Step Process Does Not Infringe Any of the Licensed Patents*
>
> *B. Because the Ohmeda Three-Step Process Does Not Infringe Any Licensed Patent, Neither Maruishi Nor Abbott Has Any Rights to That Process*
>
> *1. The Patent Grant in the 1992 License Agreement Only Extends to Technology That Is Covered By the Claims of the Licensed Patents*
>
> *2. The Know-How Grant in the 1992 License Agreement is Similarly Limited in Scope*
>
> *C. Because the Language of the 1992 Baxter/Maruishi Agreement is Clear on this Point, the Tribunal May Not Consider Extrinsic Evidence to Alter the Meaning of the Contract*
>
> *D. If the Tribunal Were Nevertheless to Consider Extrinsic Evidence, the Extrinsic Evidence Supports Baxter's Position*
>
> *E. Abbott Has No Standing to Seek Arbitration Regarding Baxter's Satisfaction of Its Patent and Know-How Grants to Maruishi*
>
> *II. Baxter has not breached any representation that it made in the 1992 agreement with Maruishi*
>
> *III. Abbott's invocation of the Parties' Original Commercial Relationship' is misconceived*
>
> *IV. Abbott's miscellany of other legal theories also lack merit*

A. Abbott's Promissory Estoppel Claim is Meritless

B. Abbott's Legal Estoppel Claim is Meritless

C. Abbott's Unfair Competition Claim is Meritless

D. Baxter Has Satisfied Its Duty of Good Faith and Fair Dealing

V. Abbott's construction of the 1992 Baxter/Maruishi License Agreement, if adopted, would raise serious antitrust concerns"

§14.- These claims and defences raised some significant factual questions, particularly relating to the degree of similarity between the process protected by the 334 and 898 Patents, on the one hand, and the 239 Patent on the other, and whether the 239 Patent is an 'improvement' or involved the use of '*Know-How*' relating to the 334 and 898 Patents. There were also important factual questions relating to the Parties' representations and intentions. Accordingly, the Tribunal held five days of evidence (including cross-examination) of witnesses, followed by closing arguments. Of particular importance was the scientific evidence of Dr. Richard Lagow, a renowned fluorine chemist and a professor of the University of Texas on behalf of Abbott, and Dr. Ralph Lessor, an organic chemist and Associate Director of Chemistry at Baxter Laboratories in New Jersey, and also one of the named inventors of the 239 Patent. The Tribunal has also had the benefit Post-Hearing Briefs from both the Parties.

VIII. *REASONS*

§15.- The Tribunal proposes to provide its reasons under six headings:

(a) Abbott's Right to Bring an Action on the Baxter/ Maruishi Agreement.

(b) The Baxter/Maruishi Agreement;

(c) The Dispute Resolution Agreement;

(d) The Duty of Good Faith;

(e) Promissory Estoppel;

(f) Antitrust Issues.

(a) Abbott's Right to Bring an Action on the Baxter/ Maruishi Agreement.

§16.- Abbott is not a signatory to the Baxter/Maruishi Agreement. It claims however that it has rights under the Baxter/Maruishi Agreement as a third parry beneficiary. In its Response to the Notice of Dispute, Baxter took the position that Abbott was definitely not third party beneficiary of the Baxter/Maruishi Agreement, and had no general standing to sue for its breach. Baxter's counsel repeated this argument in Baxter's final submissions at the hearing on March 8, 2000.

§17.- It is clear that under Illinois law that a third party beneficiary has a right to sue for breach of contract. The rule is stated by the Supreme Court of Illinois in *Carson Pirie Scott & Co v Parrett* 178 N.E. 2d 498 (1931) (*see also F. W Hempel & Co Inc v Metal World, Inc.* 721 F 2d. 610 (7th Circ. 1983):

> "*The rule is settled in this state that, if a contract be entered into for a direct benefit of a third person not a party thereto, such third person may sue for breach thereof. The test is whether the benefit to the third person is direct to him or is but an incidental benefit to him arising from the contract. If direct, he may sue on the contract; if incidental he has no right of recovery thereon. This rule has been announced without variation in numerous cases decided by this court.*"

The Supreme Court of Illinois made clear that whether a benefit was direct or not depended on the intention of the parties "*as that intention is to be gleaned from a consideration of all of the contract and the circumstances surrounding the parties at the time of its execution.*"

§18.- The Tribunal finds that the intention of Baxter and Maruishi at the time of the Baxter/Maruishi Agreement was to confer a direct and not an incidental benefit upon Abbott. The recitals to the Baxter/Maruishi Agreements made clear that this agreement was made for the purpose of implementing a wider set of arrangements involving Abbott. There are numerous express references to Abbott within the operative clauses of the Baxter/Maruishi Agreement and a specific clause (clause 5) devoted to matters relating to the covenants that Maruishi was required to obtain from Abbott in the Abbott/Maruishi Agreement. Clause 6 of the Baxter/Maruishi Agreement contained a series of representations and warranties by Baxter relating to their rights to and the status of the Licensed Patents that were clearly intended for the benefit of Abbott as well as Maruishi, as the protection of these warranties was imperative for Abbott's investment in and development of Sevoflurane. Clause 10 gives Abbott an express right to invoke the Dispute Resolution Agreement if it reasonably believes that a dispute threatens to result in an Impairment of the Original Commercial Relationship. Finally, the Dispute Resolution Agreement itself, which relates to all the Sevoflurane Agreements and which establishes that these Agreements together form an "*Original Commercial Relationship*", confirms the clear intention of the parties to enter into the Baxter/Maruishi Agreement for the direct benefit of Abbott.

Accordingly, Abbott has a right to sue on the Baxter/Maruishi Agreement in Illinois law on the basis that it is a third party beneficiary of this agreement.

(b) The Baxter/Maruishi Agreement

§19.- The critical contractual provision of this agreement is clause 2.0 entitled "*License Grants*". In clause 2.1 Baxter grants an exclusive license to Maruishi, even as to Baxter under the "*Licensed Patents and any improvements thereon to make, . . . Sevoflurane and HFIP . . . , with rights to*

sublicense". Following this grant, the terms Sevoflurane and HFIP are defined: "*Sevoflurane and HFIP*" shall mean Sevoflurane and HFIP *manufactured using a process that but for the license granted herein would infringe one or more of the Licensed Patents.* This is standard language used in patent licenses to make clear the scope of the rights yielded by the patent holder or licensor and, by the same token, specifically identifies the rights the licensee is receiving, for which it must pay royalties. In this case the licensor, Baxter, is not only giving up all rights to the Licensed Patents, but also granting Maruishi rights to any 'improvements' on the Licensed Patents. This adds to the grant, but only insofar as the 'improvements' directly related to Licensed Patents—nothing more.

In Clause 2.3 Baxter makes a further grant to Maruishi an of exclusive license even as to Baxter to "*use the Know-How and any improvements thereon to make, use . . . Sevoflurane and HFIP . . . with rights to sublicense . . .*". Know-How is defined in clause 1.1 (see §7 above). In this definition, the grant of Know-How is tied to the defined terms '*Sevoflurane and HFIP*'. Therefore, the grant of Know-How is related and bound to the Licensed Patents and the technology disclosed therein. In brief, the critical grant clauses make clear that all Baxter grants and everything that Maruishi receives is tied tightly and clearly to the Licensed Patents and related improvements and Know-How (hereinafter referred to collectively as the "*Licensed Technology*").

The Licensed Patents all relate to the so-called one-step process for manufacturing Sevoflurane. Thus, only if the three-step process infringes one of the Licensed Patents, or is an improvement on the one-step process, or developed from Know-How relating to the one-step process do the express terms of the Baxter/Maruishi Agreement forbid Baxter from using the three-step process to manufacture Sevoflurane and HFIP in competition with Maruishi or Abbott.

§20.- There is no proof in the record that the new Baxter three-step process infringes any of the four Licensed Patents. Abbott instead sought to prove that the 239 Patent used the Licensed Technology, or constituted an 'improvement' of the Licensed Technology within the meaning of 'improvement' in clause 2 of the Baxter/Maruishi Agreement.

§21.- The Tribunal finds, on the basis of the evidence presented at the hearing, that the three-step process was not an improvement on the one-step process. There may be similarities between the two processes, but the Tribunal considers that the two processes have enough technical differences to conclude that the three-step process not only does not infringe the patents relating to the one-step process, but is not technically similar to the one-step process.

Further, the Tribunal finds that the three-step process did not use any Know-How from the one-step process. By the time Baxter acquired Ohmeda, the three-step process had already been developed. The evidence establishes that Ohmeda developed the three-step process using publicly available information relating to the Baxter expired patents. These patents expired prior to the Baxter/Maruishi Agreement. As such, these patents were not part of the Licensed Technology and Baxter's rights in know-how relating to these unlicensed patents was not granted to Maruishi by the clause 2.3 grant of the Baxter/Maruishi Agreement.

§22.- Accordingly, the Tribunal finds that, Baxter was under no obligation under the Baxter/Maruishi Agreement to transfer Know-How or improvements relating to the 239 Patent, as the 239 Patent did not infringe the Licensed Patents nor did it use any other Licensed Technology. Maruishi/ Abbott had not paid for and were not entitled to the information Baxter had on the three-step process, which was developed totally independently of the one-step process.

(c) The Dispute Resolution Agreement

§23.- In Abbott's submission Baxter's proposed entry into the Sevoflurane market would impair the Original Commercial Relationship as this term is defined in the Dispute Resolution Agreement. This, Abbott alleges, is a breach of the Dispute Resolution Agreement.

In Baxter's submission the Dispute Resolution Agreement created no independent obligation on the Parties to maintain their Original Commercial Relationship. Rather, it required that in the event of a breach of one of the other Sevoflurane Agreements, then a remedy was to be selected to restore the Original Commercial Relationship. In Baxter's submission without a breach of one of the other Sevoflurane Agreements, there is no need to consider the Original Commercial Relationship at all.

§24.- The Tribunal notes at the outset that clause 8.9 of the Dispute Resolution Agreement provides:

> "*The headings and recitals appearing in this Agreement have been used for reference purposes only and will not affect the interpretation or enforcement of this Agreement.*"

In accordance with this clause, the Tribunal cannot refer to the definition of '*Original Commercial Relationship*' in Recital F of the Dispute Resolution Agreement.

The Dispute Resolution Agreement is closely connected to the Sevoflurane Agreements. Clause 10.1 of the Baxter/ Maruishi Agreement stipulates:

> "*The Parties acknowledge that under the Dispute Resolution Agreement, either party or Abbott or Central Glass will have the right to invoke the Dispute Resolution Agreement and proceed in accordance with the provisions thereof, . . . if such party or Abbott or*

> *Central Glass reasonably believes that Impairment of the Original Commercial Relationship will result from the dispute between the parties. . .*"

'*Impairment of the Original Commercial Relationship*' is defined in clause 1 of the Dispute Resolution Agreement (see §10 above). This provision establishes that any party can invoke Dispute Resolution Agreement if a party believes that a dispute between the parties could result in an impairment of the Original Commercial Relationship. A breach of one of the Sevoflurane Agreements is not required to invoke Dispute Resolution Agreement. A dispute on any of the Sevoflurane Agreements that could result in the Impairment of the Original Commercial Relationship is all that the Dispute Resolution Agreement requires.

§25.- Accordingly, in the Tribunal's view, the Dispute Resolution Agreement contains an independent obligation (and therefore cause of action) to prevent any Impairment of the Original Commercial Relationship (see the emphasised words in §10 above). Any Impairment of the Original Commercial Relationship is a breach of the Parties' obligations.

§26.- Baxter's sales of a generic Sevoflurane product will "*reduce the amount a party would but for such change otherwise receive under any Sevoflurane Agreement.*" (clause (a)(iii) of the definition of Impairment of the Original Commercial Relationship in §10).

Baxter admitted in a letter dated January 18, 1999 from Mr. McGinley to Maruishi (Abbott Exhibit 23) that its entry into the market would disrupt the Original Commercial Relationship among the parties. Should Baxter re-enter the market with a generic Sevoflurane, Abbott's sales of Sevoflurane will be affected thereby adversely affecting the overall economic benefit, not only for Abbott, but also Maruishi and Central Glass.

On this basis Baxter should be enjoined from selling a generic Sevoflurane product through the term of the Baxter/Maruishi Agreement; that is until June 2005, as this conclusion will maintain Original Commercial Relationship.

(d) The Duty of Good Faith

§27.- Abbott has argued that Baxter has a duty of contractual good faith, and it would be a breach of this duty to enter into competition with its own sublicensee, thereby preventing Abbott enjoying the fruits of the Sevoflurane Agreements and also impairing the Original Commercial Relationship.

It is Baxter's position that, as a matter of Illinois law, the duty of good faith does not create an independent cause of action, and therefore provides no basis for relief separate and apart from Abbott's breach of contract claims. Baxter also argues that as a matter of fact, Abbott has received the full fruits of the Sevoflurane Agreements, and in fact has received actual profits on the sale of Sevoflurane up to 2000 of at least $450 million, or nearly triple the amount to be expected.

§28.- In the United States the contractual duty of good faith appears in various contractual texts, including the Uniform Commercial Code, the American Law Institute Restatement (2d) of Contracts and the UN Convention on Contracts for the International Sale of Goods (ratified by the United States). While the existence of the duty is acknowledged, its scope and meaning have produced vigorous, academic debate and a 'tangled' case law. One of the major questions of practical importance relating to the doctrine of good faith in the United States is the very legal question raised in this arbitration; that is, whether the duty gives rise to an independent cause of action (see generally E. Allan Farnsworth, '*Good Faith in Contract Performance*' in Beatson and Friedmann '*Good Faith and Fault in Contract Law*' (Oxford, 1995)).

The Parties have both cited relevant authorities in their briefs in support of their respective position on whether breach of the duty of good faith creates an independent cause of action in Illinois law. The reasoning in these authorities is not detailed and their conclusions are irreconcilable. The Tribunal can only conclude that an independent cause of action for breach of duty of good faith exists in some circumstances under Illinois law, but whether it exists in a particular case depends upon the nature of the contract between the parties, and the appropriateness of the duty in the context of the relationship between the parties.

§29.- The relationship between the Parties under the Sevoflurane Agreements involves a long term licence arrangement. Abbott, as sublicensee, was required to make an investment of many millions of dollars to secure the benefits of the contract. A long term relationship of this nature requiring considerable investment is an appropriate contract for an enforceable obligation of good faith. There are two authorities at Federal Court of Appeal level—although not applying Illinois law—that strongly endorse an enforceable duty of good faith in franchise agreements where the franchisor has entered into competition with its franchisee and deprived it of the fruits of the contract. There is a strong analogy between the position of the franchisee in these cases, and that of Abbott under the Sevoflurane Agreements (see *Camp Creek Hospitality Inns v Sheraton Franchise Corporation* 139 F.3d 1396 (11th Circ. 1998) and *Vylene Enter Inc v Naugles Inc 90* F.3d 1472 (9th Circ. 1996)).

§30.- It is axiomatic that the application of the duty of good faith in a contract must not contradict the express provisions of the contract. Abbott in the present case asserts that the duty of good faith prevents Baxter from entering the Sevoflurane market with a generic product. A proper interpretation of the definition of "*Sevoflurane and HFIP*" in clause 2.1 of the Baxter/Maruishi Agreement, and the

application of this expression throughout this agreement, establishes that Baxter never expressly agreed not to sell Sevoflurane made by a different process. It is equally true, however, that Baxter nowhere in the Agreement reserved itself the right to compete with its licensee or sublicensee using a generic Sevoflurane. The Sevoflurane Agreements are completely silent on the very important issue of competition by Baxter and therefore the application of the duty of good faith in no way contradict the express terms of the Sevoflurane Agreements.

In fact there are a number of indications within the Sevoflurane Agreements that the Parties had an expectation of mutual performance in good faith. Clause 6.1 of the Baxter/Maruishi Agreement contains an express obligation of good faith in respect of the subsequent negotiation of the Dispute Resolution Agreement, and also obligations to cooperate (clauses 5.2 and 8.0) and to use reasonable efforts (clause 7.0). In the context of the specification manifestation of the duty of good faith involved in this case, it is also important to refer to clause 3.6 of the Baxter/Maruishi Agreement:

> "*3.6 Under this Agreement Baxter has no right or ability to affect the actual selling price of Sevoflurane or HFIP sold by Maruishi or Abbott.*"

This clause does not go so far as to impose on Baxter an express duty not to affect the actual selling price of Sevoflurane or HFIP, but does recognise an expectation that Baxter will not assert any right or ability to affect the selling price of Sevoflurane or HFIP, and this expectation is consistent with, and can be given effect to by, an obligation of good faith.

The existence of a positive obligation of good faith amongst the parties to the Sevoflurane Agreements is confirmed by the repeated references to the duty of good faith in the Dispute

Resolution Agreement (see clauses 2.1, 2.2, 4, and 7.3). Further, the express obligations of the Parties to preserve the commercialisation of Sevoflurane and the Original Commercial Relationship support the conclusion of an obligation of good faith.

§31.- Accordingly, this Tribunal finds that the obligation of good faith under Illinois law in this case establishes an independent cause of action under the Baxter/Maruishi Agreement. In the circumstances of the Sevoflurane Agreements, good faith is not only an aid in the interpretation of the Agreements, but is a distinct legal basis for contractual commitments.

§32.- The next question is whether there has been a breach of the obligation of good faith on the facts presented in evidence. Baxter argued that Abbott had received the full benefit of the bargain it struck in 1992, and that Abbott expected to face generic competition as soon as the Food and Drug Administration period of exclusivity expired in 2000. This may be so, but is beside the point. It is a breach of the duty of good faith for Baxter to deprive its own sublicensee of the fruits of its contract, even though an independent third party might do so with impunity. The bad faith character of Baxter's proposal to enter the Sevoflurane market only becomes more clear when one considers it not only will hurt Abbott, but will also reduce Baxter's only royalties from Abbott's sales.

(e) Promissory Estoppel

§33.- Abbott also advanced various arguments under a theory of promissory estoppel, alleging that Baxter executives represented to Abbott during the negotiation of the Sevoflurane Agreements that Baxter "*was leaving the business, that Baxter was not interested in Sevoflurane, they were not interested in exploring—exploiting or participating in the inhalation market*". Abbott claims that it relied on this

promise, that its reliance was expected and foreseen by Baxter, and that Abbott will suffer detriment as a result if Baxter now enters the Sevoflurane market. Baxter's position was that there was no unambiguous promise—as required by Illinois law—that Baxter would not sell Sevoflurane during the life of the Baxter/Maruishi Agreements, and that under Illinois law Abbott's promissory estoppel claim is barred by the fact that the Parties subsequently entered into the written contractual arrangements contained in the Sevoflurane Agreements and the Dispute Resolution Agreement.

The Tribunal considers that the duties of the Parties are determined by the actual contractual relationship agreed by the Parties in the Sevoflurane Agreements and the Dispute Resolution Agreement, including the obligation of good faith that was part of this contractual relationship. Abbott cannot rely on oral promises not reflected in these agreements, and therefore the promissory estoppel claim is dismissed.

(f) Antitrust Issues

§34.- Baxter submitted that any agreement between Baxter and Abbott that had the effect of preventing Baxter from entering the Sevoflurane market with a generic product would have severe anticompetitive implications injurious to consumers, and therefore would be illegal under United States antitrust law. Abbott submitted that Baxter's evidence was based on flawed assumptions and failed to prove any kind of antitrust violation, and that in addition the parties, including Baxter, had considered and analysed the antitrust laws in 1992 and had concluded that the Sevoflurane Agreements were legal.

§35.- The Tribunal accepts Abbott's argument on this question. It considers that no illegality results from the interpretation of the Sevoflurane Agreements in this Award. Baxter's evidence assumed that that the Sevoflurane Agreements obligated Baxter to licence the three-step process

to Abbott, whereas this Tribunal considers that the three-step process is not included in the licence granted to Maruishi and sublicensed to Abbott under the Sevoflurane Agreements (see §§19-22 above). This is not a case of the Sevoflurane Agreements having any competitive implications that were not foreseeable by the Parties in 1992 when generic competition was expected after December 2000, and Baxter has not established that such competition is not still possible. The apparent antitrusts issues relating to the Sevoflurane market that Baxter now seeks to rely upon to escape its contractual obligations under the Sevoflurane Agreements do not arise from those Agreements themselves, but as a result of Baxter's acquisition of Ohmeda and the 239 Patent, which removed from the Sevoflurane market the very type of independent generic competitor foreseen by the Parties in 1992.

IX. *COSTS*

§36.- Rule 16 of the CPR Rules requires the Tribunal to fix its costs in the award. In accordance with clause 7.6 of the Dispute Resolution Agreement, the fees, costs and expenses of the Tribunal shall be borne equally by the Parties. The Parties shall also each bear their own costs.

X. *AWARD*

In light of the foregoing and having taken cognisance of all claims and defences raised by the Parties in their written and oral submissions, and all evidence and testimony presented to the Tribunal, THIS TRIBUNAL HEREBY DECIDES THAT:

1. Baxter International Inc is hereby ordered not to market, whether directly or indirectly, the inhalation anaesthetic known as Sevoflurane in the Territory defined in the Sevoflurane Supply and License Agreement Between Maruishi Pharmaceutical Co. Ltd and Abbott Laboratories dated September 4, 1992, until the expiration or termination of that Agreement;

2. Each party shall pay one-half of the fees, costs and expenses of the Arbitral Tribunal.

This Final Award is made (by a majority) in the cities referred to below for Chicago, Illinois, United States of America, this 15th day of June 2001:

FOR AND ON BEHALF OF THE ARBITRAL TRIBUNAL

/s/ Kazuo Iwasaki	/s/ Gaynell C. Methvin Esq	/s/ Bernardo M. Cremades
PROF. KAZUO IWASAKI	Gaynell C. Methvin Esq	Dr. Bernardo M. Cremades
(in Inuyama for Chicago)	(in Dallas for Chicago)	(in Madrid for Chicago)

Dissenting

CPR INSTITUTE FOR DISPUTE RESOLUTION
BINDING ARBITRATION

ABBOTT LABORATORIES

v.

BAXTER INTERNATIONAL INC.

Before Dr. Bernardo M. Cremades, Professor Kazuo Iwasaki, Gaynell C. Methvin

DISSENTING OPINION

Following the hearing in this matter, I reviewed all briefings, exhibits, transcripts of the hearing, etc. and provided the other panel members with a Memorandum which detailed my independent analysis of the issues in this matter. The basis for my dissent from the Award is found in this Memorandum which is attached hereto and incorporated herein for all purposes. It will be readily apparent from a review of this Memorandum why I disagree with the Award. In particular,

(1) For the reasons stated in the Memorandum, the conclusion in the Award that "A breach of one of the Sevoflourane Agreements is not required to invoke Dispute Resolution Agreement" (Section 24) is clearly erroneous. The Award cites as authority, Article 1 of the Dispute Resolution Agreement (the "DRA") *(see* Section 10 of the Award) which on its face clearly states that an "Impairment of the Original Commercial Relationship shall mean: (a) an alleged breach or termination of one of the Sevoflourane Agreements. . . . ." The Award provides no explanation for ignoring the plain language of the DRA nor does it attempt to contradict the analysis of the Memorandum which reaches a completely contrary conclusion as to what is required to invoke the DRA.

(2) The Award's analysis of the good faith requirements under Illinois law is likewise erroneous. The Award relies on two cases from jurisdictions other than Illinois that Abbott thought so little of that they didn't even make footnote status in Abbott's post-hearing briefing. The Illinois cases Abbott did rely on (Tabs 11 and 13) clearly state that the duty of good faith and fair dealing is a derivative principle of contract law . . . essentially used as a construction aid to determine the intent of the parties where a contract is susceptible of two conflicting constructions. The Memorandum demonstrates that the contracts in this case were not susceptible to two conflicting constructions. The Award simply ignores the Illinois law on this point.

For the foregoing reasons, I respectfully dissent from the Award.

DATED this 22nd day of June, 2001

/s/ Gaynell C. Methvin
Gaynell C. Methvin

GAYNELL C. METHVIN
ATTORNEY • MEDIATOR • ARBITRATOR

MEMORANDUM

TO:	Benardo Cremades Professor K. Iwasaki
FROM:	Gaynell C. Methvin
MATTER:	Abbott v. Baxter Arbitration
REGARDING:	Abbott Laboratories v. Baxter International, Inc.—Case Analysis
ISSUE:	Do the relevant Sevoflurane Agreements (Maruishi/Baxter License or Abbott/Maruishi Supply & License) and/or the Dispute Resolution Agreement and/or any oral agreement prohibit Baxter from competing with Maruishi or Abbott in the sale of Sevoflurane?
DATE:	April 20, 2001

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a. *GENERAL ANSWER:*

Baxter can be prevented from engaging in competition *only if* it uses a process to manufacture Sevoflurane which: (1) infringes one of the four Baxter patents licensed to Maruishi, or (2) is based on improvements to such patented technology, or (3) is based on know-how directly related to the patented technology. Stated another way, if the Baxter 3-step process is not covered by the licensed patents or based on improvements or know-how related to these licensed patents, Baxter is free to compete and neither Maruishi nor Abbott has a cause of action or legal basis to prevent such competition.

b. *CONCLUSION ON MERITS:*

Abbott has failed to prove that the Baxter three-step process (1) infringes the licensed patents; (2) is an improvement on the technology disclosed in the licensed patents; or (3) is based on know-how related to the licensed patents. Accordingly, all of Abbott's causes of action based on the written agreements must be denied. Further, there was no enforceable oral contract between Baxter and Maruishi or Abbott which would give rise to such a cause of action, nor is there any other legal basis for such a claim by Abbott to prevent competition from Baxter.

c. *SUPPORT FOR CONCLUSION:*

The approach I have taken to this problem is to review the relevant written agreements and the hearing testimony related to the alleged oral agreements, without specific references to the briefs of the parties, to determine whether, in my independent view, these written or alleged oral agreements support Abbott's position. The only relevant written agreements are the Maruishi/Baxter License Agreement (the "M/B Agreement") Maruishi/Abbott Sales and License Agreement (the "M/A Agreement"), and the Dispute Resolution Agreement (the "DRA"). In the following paragraphs, these agreements will be reviewed, analyzed and discussed first, then the alleged oral agreements will be considered. Following these sections of the memo you will find a very brief discussion of the other legal theories asserted by Abbott against Baxter.

1. *The Maruishi/Baxter Patent and Know-How License Agreement dated September 3, 1992*

   a. *The Grant Clauses.*

The first and most critical and contractually significant provision of this agreement is found in § 2.0 "License Grants." In § 2.1 we see that Baxter grants an exclusive license to

Maruishi, even as to itself under the "License Patents and any improvements thereon to make, . . . Sevoflurane and HFIP . . ., with rights to sublicense." Following this grant, the terms Sevoflurane and HFIP are defined: "'Sevoflurane and HFIP' shall mean Sevoflurane and HFIP *manufactured using a process that but for the license granted herein would infringe one or more of the Licensed Patents*." (Emphasis added.) This is standard language used in patent licenses to make clear the scope of the rights yielded by the patent holder or licensor and, by the same token, specifically identify the rights the licensee is receiving, for which it must pay royalties. In this case the licensor, Baxter, is not only giving up all rights to the Licensed Patents, but also granting Maruishi rights to any "improvements" on the Licensed Patents. Obviously, this adds to the grant, but only in so far as the "improvements" directly relate to the four Licensed Patents—nothing more.

Next, § 2.3 also serves to add to the grant in that Baxter grants Maruishi an exclusive license even as to Baxter to "use the Know-How and any improvements thereon to make, use . . . Sevoflurane and HFIP . . . with rights to sublicense . . . ." Know-How is referenced in § 1.1, but more importantly, the grant of Know-How is tied to the defined terms "Sevoflurane and HFIP." Therefore, again, the grant of Know-How is related and bound to the Licensed Patents and the technology disclosed therein. In brief, the critical grant clauses make clear that everything Baxter is giving up and everything that Maruishi is receiving is tied tightly and clearly to the Licensed Patents and related improvements and Know-How (hereinafter referred to collectively as the "Licensed Technology").

To repeat, the critical grant language of the M/B Agreement defines Baxter's rights for the future and makes it clear exactly what Baxter is giving up, *i.e.*, Sevoflurane and HFIP made by any process related to the Licensed Technology.

Without going into the details of the technology disclosed in the Licensed Patents, there can be no dispute about the fact that the Licensed Patents all relate to the so-called "one-step process" for manufacturing Sevoflurane. Thus, only if the three-step process infringes one of the Licensed Patents, or is an improvement on the one-step process, or was developed from Know-How relating to the one-step process, is Baxter forbidden from using the three-step process to manufacture Sevoflurane and HFIP in competition with Maruishi or Abbott.

b. *The Royalty Clauses.*

The next section of the M/B Agreement, which is also of critical interest, is § 3 relating to payments of fees and royalties. Section 3.1 provides for four non-refundable payments totaling $6.5 Million which were to be paid over time. These are commonly known as minimum royalty payments and are the fees Baxter receives regardless of whether Maruishi ever uses the Licensed Technology.

In § 3.2 we find that Maruishi is obligated to make royalty payments based on the total quantity of "Sevoflurane and HFIP" sold. The terms "Sevoflurane and HFIP" used in this section are obviously tied to the definition of these terms found in § 2.1 for it is clear that Maruishi should not be obligated to pay royalties on any process that is not covered by the Licensed Technology.[1] This makes perfect sense of course, since Maruishi should not have to pay for technology not developed by Baxter and transferred to Maruishi by the license. Indeed, Mr. Townsend testified that he drafted and

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[1] Although I will discuss these facts more later, in my view, since Abbott elected not to attempt to prove that the Baxter three-step process was an infringement of the Licensed Patents, or related to the Know-How or improvements on the License Patents, Abbott completely failed to prove what was fundamentally necessary to win its case on the written agreements, and, accordingly, its causes of action based on the M/B Agreement should be denied.

proposed this specific definition of Sevoflurane and HFIP for inclusion in the agreement to make sure that Maruishi paid royalties to Baxter only when Sevoflurane was made using the Licensed Technology.[2] Mr. Townsend also testified that he had originally proposed that the definition be included in the royalty provision in § 3.2. Since the grant and royalty obligations are coextensive, however, it was not important whether the definition of Sevoflurane and HFIP was placed in the grant clauses or the royalty clauses. In the end the parties obviously agreed that the definition should be in the grant section in order to make perfectly clear exactly what Baxter was giving up and exactly what Maruishi was receiving. By the same token, Baxter keeps and can use anything not granted to Maruishi.

Thus, in the two most critical and determinative sections of the M/B Agreement, the terms Sevoflurane and HFIP are consistently and clearly defined, with such definition being entirely consistent with Maruishi's intent to pay royalties only if it used the Licensed Technology, but not otherwise.

I have also carefully reviewed all of the agreements in evidence to determine the impact of the § 2.1 definition of Sevoflurane and HFIP on Baxter if Maruishi, instead of Baxter, had developed and used the three-step process or any other process that did not infringe or use the Licensed Technology. My conclusion for this review is that only the M/B Agreement was relevant to the inquiry and that agreement dictates that if Maruishi had gone to the three-step process, Baxter would have received the minimum royalties

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[2] As you will recall from Mr. Townsend's testimony, Maruishi was upset that in 1992, Baxter was insisting on a royalty bearing license as opposed to their earlier option agreement which called for Baxter to receive fifty percent (50%) of profits. Thus, Maruishi wanted to make sure that if they ever used another process other than the one covered by the Licensed Technology, they would be free to do so and not owe any royalties to Baxter.

provided in § 3.1 and no other royalties from Maruishi. In addition, because it had granted an exclusive license to Maruishi, even as to itself, as to the Licensed Technology, Baxter could not, during the period of the M/B Agreement, license anyone else to produce Sevoflurane and HFIP using the Licensed Technology or do so itself. In summary, had Maruishi changed to the 3-step process, Baxter would have been left "high and dry:" (1) its royalty income stream would have terminated; (2) it would not have the right to license the patents or any of the Licensed Technology to any third party; and (3) it would not have been able to use the Licensed Technology to make, use or sell Sevoflurane and HFIP. Thus, by reason of the grant, Baxter definitely took the risk that it might never receive anything more than the minimal fees provided in § 3.1 for its Licensed Technology should Maruishi at any time switch to a non-infringing process.[3]

By the same token, the only legally correct and fair interpretation of the M/B Agreement is that it was not just Baxter who took a risk regarding future use of a non-infringing process. As I see it, Maruishi also took the risk that Baxter, at some point, might develop, or buy and use a process for making Sevoflurane and HFIP that was not covered by the Licensed Technology. In that event, Baxter would be just as free as Maruishi to use such a non-infringing process. If it did so, Baxter would be free to sell a generic product in competition with Abbott and neither Maruishi nor Abbott would have any basis under the M/B Agreement to prevent such competition. This risk existed for Maruishi and Baxter regardless of their awareness of the ramifications of the terms of the M/B Agreement. I am confident, however,

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[3] As an aside, I note that Abbott's comments that Baxter was merely a "cash collector," implying that Baxter made no contribution, is absurd. Baxter developed and patented the one-step process. Without Baxter's contribution, Abbott would never have generated the billion dollars in revenue it received for its sales of Sevoflurane.

that a person of Mr. Townsend's capabilities in this field understood this risk and advised his client to take the risk.

b. *Other Uses of the Terms "Sevoflurane" and "HFIP" in the Sevoflurane Agreements Other than as Defined in § 2.1 of the M/B Agreement.*

Not only are the separate terms "Sevoflurane" and "HFIP" used numerous times in the M/B Agreement, they are also used numerous times in the M/A Agreement, and the DRA. In my opinion, these terms are used in a clear and consistent fashion throughout all of the written agreements. It was not necessary for the defined terms "Sevoflurane and HFIP" *(see* §§ 2.1, 2.3 and 3.2 of the M/B Agreement) to be used throughout the Sevoflurane Agreements and the DRA. When the individual terms "Sevoflurane" and "HFIP" are used repeatedly throughout these agreements, they are used merely to identify the product at issue and are not used, as in § 2.1 or the M/B Agreement to create legally enforceable rights or remedies. Again, I find the individual terms to be used very consistently, and used in a fashion that makes it clear that they are being used for a purpose other than identifying legal rights or remedies. Such consistency of use is what one would expect in light of the history of the negotiation process that led to the ultimate signing of these commercial and licensing arrangements. The evidence shows that the negotiation and drafting of the agreements was conducted by in-house counsel and business personnel for both Abbott and Baxter. We must assume that the counsel were competent and capable attorneys accustomed to negotiating license and commercial sales agreements. Also, we know for a fact that Maruishi was represented by the highly competent and distinguished Mr. Townsend. Thus, I find—as you would expect—the terms of the agreements are not ambiguous and are used in a consistent fashion. I also find nothing in any of these agreements that would indicate that the parties left any

loopholes or ambiguities relating to any critical terms or phrases. All of the agreements reflect competent negotiation and drafting.

c. *Does the Baxter three-step process infringe of the Licensed Patents*?

As noted earlier in footnote 1, there is no proof in the record that the new Baxter three-step process infringes any of the four Licensed Patents. Indeed, in my view, it was Abbott's burden to prove such infringement, but instead of attempting to meet this burden, it elected to try to show that the two processes were very similar. This approach was flawed since the issue of whether the two processes are similar is not a relevant inquiry. Thus, Abbott left itself without any proof that the process to be used by Baxter infringes the Licensed Patents.

d. *Does the Baxter three-step process use any other Licensed Technology*?

First, as noted earlier, there was no evidence presented at the hearing to indicate that the three-step process was an improvement on the one-step process. Indeed, Abbott's witnesses agreed that the three-step process was, for obvious reasons, actually a step backwards, not forwards, from the one-step process. Again, the fact that there may be similarities between the two processes is simply not relevant. The relevant issue is whether or not the Baxter's 3-step process acquired from Ohmeda, is an improvement on the Licensed Technology. It is not. For what its worth, I find from a technological standpoint (and I do hold a degree in chemical engineering) that the two processes have enough technical differences to conclude that the three-step process not only does not infringe the patents relating to the one-step process, but is not technically similar to the one-step process. Thus, I reject Dr. LaGow's analysis and accept Dr. Lessor's analysis of the two processes.

Furthermore, the three-step process could not have used the Know-How related to the one-step process. Since the three-step process is not an improvement on the one-step process, it is very unlikely that it could have been based on any know-how relating to the one-step process. Indeed, there is no proof that the three-step process used any know-how from the one-step process. By the time Baxter acquired Ohmeda, the three-step process had already been developed! Also, the evidence is undisputed that Ohmeda developed the three-step process using publicly available information relating to the Baxter expired patents. These patents expired prior to the M/B Agreement. As such, these patents were not part of the Licensed Technology and Baxter's rights in know-how relating to these unlicenced and irrelevant patents could not have been and were not granted to Maruishi by the § 2.3 grant of the M/B Agreement. Nevertheless, for the sake of completeness, I will explore further the exact Know-How that Baxter was obligated to transfer to Maruishi.

The "Know-How" issue is of some interest, separate and apart from the other Licensed Technology, because the term could, in the abstract, be construed to include any knowledge and information Baxter possessed relating to Sevoflurane and/or HFIP, no matter where such information existed in the organization or when it got there. The M/B Agreement, however, is very specific on this issue. Baxter is well-protected by the fact that the Know-How is specifically tied to the Licensed Technology (and not anything that Baxter happens to have in its files relating to Sevoflurane). Also, the evidence indicates that Baxter transferred to Maruishi whatever Know-How it had relating to the Licensed Technology prior to 1992. There is no proof that Baxter ever acquired any know-how relating to the three-step process until after it acquired Ohmeda. But, again, this later acquired know-how did not relate to the Licensed Technology and, therefore, Baxter was not obligated to make such information available to Maruishi.

The facts indicate that Baxter had Know-How relating to the Licensed Technology used to make Sevoflurane for purposes of receiving FDA approval. In § 1.1 of the M/B Agreement, the Know-How is identified, but, as can be seen, none of this Know-How in any way relates to any aspect of the manufacturing process. However, in § 1.21 of the M/A Agreement, the terms "Technical Information and Know-How" are defined very broadly to include not only the FDA-related information (*see* § 1.21(a))—like that identified as Know-How in § 1.1 of the M/B Agreement—but also includes know-how relating specifically to the manufacturing process (*see* § 1.21(b) of the M/A Agreement).

The history of Baxter's connection to Sevoflurane manufacturing and its attempts to receive governmental approval for sale of the product, as opposed to Maruishi's history with the product makes it clear why the M/A Agreement's definition of know-how is much broader than that found in the M/B Agreement. Prior to 1983, when Baxter entered into its first agreement with Maruishi, Baxter had never gone into commercial operations, but had merely gone through Phase I Clinical Trials for FDA approval. Thus, it is understandable that while Baxter may have had data relating to this FDA approval process, it did not have data relating to the manufacturing process. There is no proof that Baxter built and operated a manufacturing facility. In all likelihood, Baxter used laboratory procedures and laboratory-scale operations to make the product needed for the clinical trials. Such laboratory type operations, however, would not have generated meaningful process know-how for full-scale manufacturing. By the time of the 1992 agreement, however, Maruishi (and Central Glass) had experience in full-scale manufacturing of Sevoflurane and had received approval from the Japanese government for sale of the product in Japan. Thus, Maruishi (and Central Glass) had significant know-how relating to the manufacturing process, whereas Baxter had none. By 1992, it seems apparent that Baxter had

nothing new in terms of know-how to transfer to Maruishi. There was no proof at the hearing that Baxter had failed to transfer any Know-How related to the Licensed Technology. Indeed, it would have been very surprising if Baxter, without any expectation of or right to financial remuneration for its efforts (or any other motivation), had continued to work on improving the one-step process solely for the benefit of Maruishi/Abbott.

In conclusion, Baxter was under no obligation to transfer know-how or improvements relating to a process that did not infringe the Licensed Patents or use any other Licensed Technology. Maruishi/Abbott had not paid for and was not entitled to the information Baxter had on the 3-step process which was developed totally independent of the one-step process.

2. *Does the Dispute Resolution Agreement Provide Abbott With Any Causes of Action to Prohibit Baxter from Competing?*

a. *The DRA's Terms and Conditions.*

1.) *Overview*

Although Abbott strived mightily to convert the DRA into an instrument which provides independent causes of action that would be asserted to prevent Baxter from competing, there is absolutely no support in the DRA for such an interpretation. The first clue to the weakness in Abbott's arguments and exposes its overall efforts as nothing more than an attempt to rewrite the DRA is Abbott's renaming the agreement from "Dispute Resolution Agreement" to "Original Commercial Relationship Agreement" ("OCR" not "DRA"). Renaming the agreement, however, does not change the terms and conditions negotiated by the parties. Furthermore, the DRA is just exactly what its title says it is—an agreement relating to resolution of disputes. From the title, to the recitals, to each and every paragraph of the agreement,

it is clear and unambiguous that this agreement is nothing more than a detailed and unique procedure for managing disputes. The DRA tells how to resolve disputes, which arise only by reason of a breach (or termination) of one of the four Sevoflurane agreements, to ensure that during this resolution process, the commercial relationship continues, *i.e.*, product continues to be manufactured and sold, and payments made. There is nothing in the DRA which could possibly be correctly interpreted to create a cause of action for Abbott or Maruishi to prevent Baxter from competing.

2.) *Specifics*

First, Recital F, of the DRA makes it plain that the agreement is related only to resolving disputes which arise due to a breach of one of the Sevoflurane Agreements:

> "In the event of a *breach or an alleged breach* of *any of the Sevoflurane Agreements* [previously defined in Recital E as the M/B Agreement, M/A Agreement, the Central Glass/Maruishi Agreement, and the Central Glass/Abbott side letter], it is the intent of the parties to the extent reasonable: (i) *to resolve such dispute* . . . and at the same time to maintain the overall contractual relationship and overall economic benefits and risks among the parties *set forth in detail in the Sevoflurane Agreements (the Original Commercial Relationship), taking into consideration the nature of the breach by a party to a Sevoflurane Agreement and the impact thereof* [*i.e.*, the impact of such a breach] of a Sevoflurane Agreement on the Original Commercial Relationship . . . ." (Emphasis added.)

All of the remaining sections of the DRA are consistent with this goal.

In Section 1 of the DRA, we find provisions, (as the title, "*Purpose of negotiation, mediation, and arbitration*" suggests) relating to negotiation, mediation and arbitration. These are the three possible procedures that could be

employed to resolve a dispute if one arose due to a breach of one of the Sevoflurane Agreements. Throughout § 1, there are references to "taking into consideration the nature of the breach," and "resolving disputes submitted," which again emphasize that these are the conditions precedent to employing one of the procedures such as negotiation, mediation or arbitration to resolve the dispute in a manner to preserve the Original Commercial Relationship. There is nothing in the first paragraph of § 1 which could in any way be construed to create a separate cause of action of any type. Causes of action, if any, arise from breaches or terminations of the Sevoflurane Agreements, not the DRA. The second paragraph of § 1 states "an Impairment of the Original Commercial Relationship shall mean: (a) an alleged breach of . . . of one of the Sevoflurane Agreements . . . ." Again, the triggering event or condition precedent which must be found prior to addressing the impairment issue, is a breach of one of the Sevoflurane Agreements. This paragraph describes what may result in an "Impairment of an Original Commercial Agreememt" following a breach of an agreement, but it does not create a separate cause of action for any purpose including a separate cause of action which would allow Maruishi or Abbott to prevent Baxter from competing by making Sevoflurane by a process which is not covered by the Licensed Technology.

In § 2, of the DRA, entitled "Performance under the Sevoflurane Agreements," the parties are instructed in how they are to perform under the agreements during the resolution of disputes according to the DRA. Again, nothing in this section creates a cause of action. Rather, this section is just another section of the agreement relating to how business is to be conducted during the resolution of the dispute based on a breach of one of the Sevoflurane Agreements.

In § 2.2, "Direct Payments by Abbott to Baxter or Central Glass," the parties are given specific directions on making

payments "while any dispute is being resolved under this agreement." No cause of action is created in this section. Section 2.3, of the DRA, "Central Glass License Option," again relates to conduct "while any disputes are being resolved under this agreement" and does not create a cause of action of any type.

Section 3 of the DRA relates to how arbitration is to be conducted under the Sevoflurane Agreements. Once more, the section relates to arbitration as a method of resolving disputes, and does not create a cause of action.

Section 4, of the DRA, "Notice Concerning Potential Impairment of the Original Economic Relationship," is exactly what the title says—terms and conditions relating to how notice must be given once a breach of contract triggers the need for dispute resolution.

Section 5, of the DRA, "Negotiation," relates to the conduct of negotiations, the first level of dispute resolution. Again, this section does not create causes of action on behalf of anyone, but rather explains how an existing dispute is to be resolved through negotiation. Likewise, in § 6, "Mediation," and § 7, "Arbitration," which relate to the two other dispute resolution procedures available to the parties, no new and independent causes of action are created.

Finally in § 7 of the DRA, "Miscellaneous," we find the standard boilerplate provisions of the agreement. This section does not create a cause of action on behalf of Abbott or Maruishi to allow them to prevent Baxter from competing in the sale of Sevoflurane.

In conclusion, I find the terms and conditions of the DRA to be entirely consistent with the description of the DRA found in § 1.9 of the M/B Agreement: "The parties, together with Central Glass and Abbott, are entering into a dispute resolution agreement (the Dispute Resolution Agreement) *establishing a mechanism by which the parties, Abbott and*

Central Glass, will cooperate to resolve certain disputes." (emphasis added) The DRA is exactly that—a mechanism to resolve disputes—nothing more—nothing less. In the end, I find it most incredible that Abbott would seriously contend that the DRA creates an enforceable cause of action which would allow them to prevent Baxter from using a process that does not employ the Licensed Technology.

b. *Further Analysis of the "Original Commercial Relationship ("OCR")."*

The "OCR" is defined in Recital F of the DRA and relates to maintaining the "overall contractual relationship and overall economic benefits and risks among the parties set forth in detail in the Sevoflurane Agreements." Of course, as stated earlier, this means that the terms of the relevant written agreements must be reviewed to determine exactly what is meant by the "overall contractual relationship and overall economic benefits and risks among the parties." This is not a difficult or complex task.

The contractual relationship found in the M/B Agreement is simply a license of patents (and improvements and know-how related thereto) with a right to sublicense. The economic benefits and the risks of this agreement are likewise clear. Baxter receives: (a) a minimum royalty regardless of which process Maruishi uses to manufacture Sevoflurane and HFIP; (b) a running royalty if and only if Maruishi uses the Licensed Technology. Baxter also runs the risk that it may receive only the minimum royalty if Maruishi elects to use a non-infringing process or stops using the Licensed Technology. On the other hand, Maruishi, by contract, receives the exclusive right, even as to Baxter, to the Licensed Technology and the right to sublicense this technology to Abbott. Maruishi (and Abbott) also run the risk that Baxter may compete using a process that does not utilize the Licensed Technology.

Next, it is clear that the DRA does not and cannot define a contractual relationship or economic benefit per se—*i.e.*, the DRA is simply not relevant to the definition of "Original Commercial Relationship" because it is not one of the "Sevoflurane Agreements."

Finally, to fully understand the contractual relationship and economic benefit between Maruishi and Abbott, it is also necessary to review the M/A Agreement.[4] Although this document is 143 pages in length, it is not difficult to understand the contractual and economic relationship between the parties. The M/A Agreement is, first and foremost, a sales requirements contract whereby Maruishi agrees to supply Sevoflurane, and Abbott agrees to buy all of its requirements of Sevoflurane from Maruishi. Of course, it also contains a sublicense of the Baxter Licensed Technology. Therefore, the contractual relationship is two-part: a commercial sales agreement and a sublicense of the Baxter patent's, know-how and technical information (*see* Definitions 1.7, 1.13, and 1.14(a)).

The sales agreement between Maruishi and Abbott is of particular interest and importance because it specifically provides for the possibility of generic competition in the future. In particular, the payment provisions of § 3.2 provide for a reduction in the bulk price that Abbott must pay Maruishi in the event competition leads to a reduction in the Abbott's sale price. Of course, such a reduction in price would also lead to a reduction in royalties that Baxter would receive under § 3.2 of the M/B Agreement because the royalties are directly tied to Abbott's average selling price. Thus, the economic relationship defined by the M/A Agreement contemplates and provides for the possibility of

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[4] As to Baxter, this agreement does not and cannot have any binding effect. Baxter was not a party to the agreement and never received a copy. Accordingly, it cannot create a cause of action against Baxter.

competition which might lead to a reduction in Abbott's sales price, Maruishi's income and commensurate reductions in royalties paid to Baxter. Accordingly, competition from Baxter, which would no doubt drive down the price that Abbott receives for its products is, from an economic standpoint, no different than generic competition from a third party. Baxter competition would not in anyway change the economic benefits of the parties as defined by the contracts. Furthermore, it is undisputed that such competition would not change anything about the contractual relationship between Maruishi, Abbott and Baxter. Finally, Baxter competition with Abbott would not change any of the "risks" set forth in any of the Sevoflurane Agreements because (1) the risk of competition from any source is already anticipated and provided for in the M/A Agreement, and (2) Maruishi (and therefore Abbott) took the risk from the outset that Baxter might go into competition by selling Sevoflurane made by use of a non-infringing process.

Also, in § 3.6 of the M/A Agreement, the parties stated that the bulk price paid by Abbott for the Sevoflurane was intended to compensate Maruishi for its supplying of these products to Abbott, and that the license and sublicense to the intellectual property rights and improvement were designed *only* to allow Abbott to use and sell these products. Again, having Baxter as a competitor with a product made from a non-infringing process would not change either aspect of this understanding. The agreement anticipated and provided for the eventuality that competition might lead to a reduction in the bulk price received by Abbott. Such competition, regardless of the identity of the competitor, would not impact the license and sublicense agreements.

Finally, a couple of other points of interest relating to the M/A Agreement need to be discussed. First, the description of the DRA found in Recital E of the M/A Agreement is different from the description of the DRA found in § 1.9 of

the M/B Agreement. Recital E of the M/A Agreement states, "*To clarify certain rights and obligations relating to Sevoflurane and HFIP*, Maruishi, Central Glass, Baxter, and Abbott have entered into a Dispute Resolution Agreement . . . ." (Emphasis added.) This description of the DRA is consistent with Abbott's theory that the DRA is more than a dispute resolution agreement. Unfortunately for Abbott, however, this statement of the purpose of the DRA in the M/A Agreement carries no legal significance and is not binding on Baxter. In addition, it should be noted that there is nothing in the M/A Agreement that specifically requires Maruishi to use only the Baxter Licensed Technology to make Sevoflurane. Indeed, the only mention in the entire agreement relating to changes in processes is found in Section 15.2(i) (which is a part of the Central Glass representations and warranties to Abbott) whereby Central Glass obligates itself to use the process spelled out in the Baxter '334 Patent without substantial change unless it receives written approval for such a change from Abbott.

In conclusion, even if the definition of Original Commercial Relationship had a stand-alone meaning and implied that Abbott was entitled to bring a cause of action against Baxter to maintain that relationship, the contractual relationships as defined by the Sevoflurane Agreements, have not been breached by Baxter. Further, the overall economic benefits and risks to the parties remain unchanged when Baxter sells Sevoflurane made by the 3-step process!

3. *Was There An Enforceable Oral Agreement by Baxter to Abbott and/or Maruishi to Not Compete in the Sale of Sevoflurane Until the Year 2005*?

It defies logic, common sense, custom and practice in the industry and controlling Illinois law to contend that the parties to this transaction would have left something as important as an agreement by Baxter to not compete to be defined by an oral understanding. Parties of the size and

sophistication of Abbott and Baxter simply do not and cannot operate in this fashion. In connection with the agreements at issue in this case, we find the parties followed a predictable pattern. They negotiated a complex written commercial and license agreement over an extended period of time, which included numerous drafts of the agreement! They, along with Maruishi, were represented by competent counsel. Likewise, the parties' business people were sophisticated and experienced in negotiating agreements like the Sevoflurane Agreements (even if the DRA was unique). Thus, it defies belief that either Abbott or Baxter, from a corporate standpoint, would have ever expected or intended that an agreement not to compete would be found in spontaneous oral conversations between corporate representatives over dinner or at some other meeting where such an agreement was not even on the agenda. While there is no reason to question Sean Murphy's testimony, to the effect that Baxter representatives indicated an intention of getting out of the Sevoflurane business forever, such statements are not tantamount to an agreement by the Baxter International, Inc, to not compete. This is especially true where the written agreements, such as here, allowed Baxter to get back in the business using unlicensed technology. Competition among major pharmaceutical corporations, such as Abbott and Baxter, is intense and ongoing, and certainly if one party was going to stay out of the business and agree not to use technology unrelated to the Licensed Technology, such an agreement would have been thoroughly considered, vigorously negotiated, reviewed and drafted by counsel and most certainly reduced to writing. In addition, even though, in my view of the facts, it is not necessary to reach the antitrust issues, clearly, an agreement to not compete in Sevoflurane or HFIP regardless of whether the Baxter Licensed Technology was used or not, would have raised antitrust issues that would have required a written legal opinion endorsing the legality of such an agreement. The record is completely devoid of any of the foregoing evidence,

which would be necessary to lend any credibility to Abbott's position that Baxter agreed not to compete until 2005.

Abbott has also argued, that it would have never entered into this transaction in the first place if it ever thought that Baxter could compete. If a noncompetition agreement from Baxter was that important to Maruishi or Abbott, however, they should have tried to negotiate a written noncompetition agreement. Abbott made the business decision not to review or have access to the M/B Agreement and apparently never even asked about the issue of competition by Baxter. Abbott relied upon Maruishi's highly competent counsel, Mr. Townsend, to ensure that there was consistency between the M/A Agreement and M/B Agreement. Mr. Townsend did his job as competent counsel. There is consistency among the agreements in the use of the terms, in defining what the parties agreed to, and what the parties did not agree to. Mr. Townsend also testified that the issue of obtaining a non-competition agreement from Baxter was never even raised. According to Mr. Townsend, it was not plausible to try to negotiate such an agreement and that in the end, Maruishi was satisfied that it had everything it needed in the existing written agreement. Of course, what Maruishi wanted, needed and received was an agreement that permitted Maruishi to use a non-infringing process to make Sevoflurane and, thereby, terminate payment of royalties to Baxter. It got what it needed, but in the process, it left open the door for Baxter to also use a non-infringing process and go in competition. Maruishi, and therefore Abbott, ran the calculated risk that Baxter might also in the future produce Sevoflurane by use of a process that did not involve the Licensed Technology. Thus, the competition from Baxter that Abbott is now complaining about was a possibility from the outset. Whether known or not, it was a risk that Abbott assumed because Maruishi assumed that risk. Abbott's knowledge of this risk is totally irrelevant, as Abbott left the specific contract provisions in this respect to be negotiated between Maruishi and Baxter.

Abbott never even attempted to negotiate a specific non-competition agreement or any other substantive agreement with Baxter.

Thus, Abbott's assertion that it would not have ever entered into the business had it known that Baxter could compete, is a problem that it should have been addressed and solved through negotiation and receipt of a written agreement. Abbott did not attempt such negotiation and didn't insist on knowing the extent of the license grant or how Sevoflurane and HFIP were defined in the M/B Agreement. Accordingly, it has no legitimate complaint about now having to suffer competition from Baxter. Furthermore, Abbott always knew there was a strong possibility of generic competition, and having anticipated this likelihood, made sure that its payments to Maruishi would be reduced if its sales price was reduced by reason of such competition. The fact that Baxter is now competing, as opposed to some third party, does not change the fact that Abbott has received the full benefit of its bargain as negotiated and spelled out in the written agreements.

d. *ABBOTT'S REMAINING CAUSES OF ACTION*

In Abbott's Post-hearing brief, it asserts that (1) "Baxter cannot compete with Abbott for Sevoflurane sales under the theory of promissory estoppel" (Abbott brief page 20) and (2) Baxter is guilty of "Unfair competition" (Abbott brief page 22).

On both the facts and the law on these two issues, I agree with Baxter's analysis contained in its post-hearing brief (pages 10 and 21) and see no reason to elaborate further on these issues for the moment.

e. *CONCLUSION*

Abbott has no basis in fact or law to prevent Baxter from competing with Abbott in Sevoflurane sales and its claims must all be dismissed.

APPENDIX D

UNITED STATES COURT OF APPEALS,
SEVENTH CIRCUIT

No. 02-2039

BAXTER INTERNATIONAL, INCORPORATED,
Plaintiff-Appellant,

v.

ABBOTT LABORATORIES,
Defendant-Appellee.

April 10, 2003

Before CUDAHY, POSNER, COFFEY, EASTERBROOK, RIPPLE, KANNE, DIANE P. WOOD, EVANS, and WILLIAMS, Circuit Judges.*

Plaintiff-appellant filed a petition for rehearing and rehearing en banc on January 30, 2003. A vote of the active members of the court was requested, Circuit Judges Ripple, Diane P. Wood, and Williams voted to grant rehearing en banc, and a majority of the judges voted to deny rehearing en banc. A majority of the judges on the panel voted to deny rehearing. The petition for rehearing is therefore denied.

RIPPLE, Circuit Judge, with whom DIANE P. WOOD and WILLIAMS, Circuit Judges, join, dissenting from the denial of rehearing en banc.

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* Chief Judge Flaum and Judges Manion and Rovner did not participate in consideration of this matter.

It is my judgment that the scope of judicial review of arbitral decisions that, at least arguably, order the parties to violate the law is an important issue that deserves the attention of the full court. As the cases cited by the dissent demonstrate, the panel opinion's analysis is difficult to square with existing Supreme Court precedent and, indeed, with the precedent of this circuit and our sister circuits.

In the panel majority's view, "the initial question is whether Baxter is entitled to reargue an issue that was resolved by the arbitral tribunal." *Baxter Int'l, Inc. v. Abbott Labs.*, 315 F.3d 829, 831 (7th Cir.2003). The panel majority takes the view that the resolution of the question is a clear-cut application of existing law. In its analysis, the panel majority first notes that *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 105 S.Ct. 3346, 87 L.Ed.2d 444 (1985), held that antitrust issues can be arbitrated. It then invokes the general principle that a mistake in law is not a ground on which to set aside an award. Consequently, the majority concludes, there is no reason to disturb the arbitral award even if the arbitral panel erred in concluding that the parties' agreement did not violate the antitrust laws.

However, as the dissent notes, the majority opinion is anything but a straightforward application of circuit and Supreme Court precedent; indeed, the majority opinion significantly expands the Supreme Court's holding in *Mitsubishi:*

> Now, the majority has taken the process one giant step further and has found that *Mitsubishi* not only allows submission of statutory and antitrust claims to arbitration, but denies our prerogative to refuse to enforce awards that command unlawful conduct . . . .

Id. at 836.

Although the majority's opinion is subject to different interpretations, there is certainly strength in Baxter's submission that, as written, the panel's opinion holds that "[a]rbitrators have the unreviewable authority to decide for themselves whether they are commanding the parties to violate the law." Rehearing Pet. at 8. There is also ground for agreeing with Baxter that such a broad holding conflicts with any number of Supreme Court and circuit cases that establish that questions of public policy are ultimately reserved for the courts. *See, e.g., W.R. Grace & Co. v. Local Union 759, Int'l Union of United Rubber, Cork, Linoleum & Plastic Workers of America,* 461 U.S. 757, 103 S.Ct. 2177, 76 L.Ed.2d 298 (1983). The Supreme Court has held that a court may refuse to enforce an arbitral award "where the contract as interpreted would violate some explicit public policy that is well defined and dominant"; this requirement is to be determined "by reference to the laws and legal precedents and not from general considerations of supposed public interests." *United Paperworkers Int'l Union v. Misco, Inc.,* 484 U.S. 29, 43-44, 108 S.Ct. 364, 98 L.Ed.2d 286 (1987) (internal quotation marks and citations omitted). This requirement—reference to an explicit public policy grounded in law—certainly is met in the present case because the policy is contained in § 1 of the Sherman Act.

Arbitration is an ever-expanding means of resolving conflicts without incurring the increased expenditure of time and funds often associated with litigation. With due respect to parties' choice of decisionmakers and also to legislative policies favoring arbitration, the role of the courts to interpret and uphold the law should not be dismissed casually. The opinion of the panel majority clouds the authority of the court to review arbitration agreements of private parties that violate public policy—an authority repeatedly acknowledged by the Supreme Court. I would grant rehearing en banc.

APPENDIX E

THIS DISPUTE RESOLUTION AGREEMENT (this "Agreement"), dated as of the Effective Date (as defined below), is among Abbott Laboratories, an Illinois corporation ("Abbott"), Baxter International Inc., a Delaware corporation ("Baxter"), Central Glass Co., Ltd., a Japanese corporation ("Central Glass"), and Maruishi Pharmaceutical Co., Ltd., a Japanese corporation ("Maruishi").

RECITALS

A. Baxter and Maruishi have entered into that certain Patent and Know-How License Agreement, dated September 3, 1992 (the "Baxter/Maruishi Agreement").

B. Abbott and Maruishi have entered into that certain Sevoflurane Supply and License Agreement, dated as of the Effective Date (the "Abbott/Maruishi Agreement").

C. Central Glass and Maruishi have entered into that certain License and Manufacturing Agreement, dated as of the Effective Date (the "Central Glass/Maruishi Agreement").

D. Central Glass and Abbott have entered into that certain Side Letter Agreement, dated as of the Effective Date (the "Central Class/Abbott Side Letter").

E. Each of the Baxter/Maruishi Agreement, the Abbott/Maruishi Agreement, the Central Glass/Maruishi Agreement and the Central Glass/Abbott Side Letter (singularly, a "Sevoflurane Agreement" and collectively, the "Sevoflurane Agreements") contains a provision requiring that the parties thereto submit to binding arbitration any disputes arising thereunder (individually, an "Arbitration Clause" and collectively, the "Arbitration Clauses").

F. In the event of a breach or an alleged breach of any of the Sevoflurane Agreements, it is the intent of the parties to the extent reasonable: (i) to resolve such dispute in a manner

that will maintain the commercialization and marketing of Sevoflurane throughout the Territory (as defined in the Abbott/Maruishi Agreement) (the "Commercialization of Sevoflurane") and at the same time to maintain the overall contractual relationship and overall economic benefits and risks among the parties set forth in detail in the Sevoflurane Agreements (the "Original Commercial Relationship"); taking into consideration the nature of a breach by a party to a Sevoflurane Agreement and the impact thereof on the Original Commercial Relationship; and (ii) during the interim period while such dispute is being resolved, to continue the Commercialization of Sevoflurane and preserve the Original Commercial Relationship, all in accordance with the terms hereof.

ACCORDINGLY, the parties agree as follows:

1. *Purpose of Negotiation, Mediation and Arbitration.* It is the intent of the parties in entering into this Agreement that the provisions hereof be applied in such a way so as to maintain to the extent reasonable the Commercialization of Sevoflurane and, at the same time, to maintain, to the extent reasonable, taking into consideration the nature of a breach by a party to a Sevoflurane Agreement and the impact thereof on the Original Commercial Relationship, the Original Commercial Relationship. The parties hereby agree that, during the course of any negotiations, mediation or arbitration conducted pursuant to this Agreement or any of the Sevoflurane Agreements, they shall seek to achieve these goals and the parties hereby instruct all negotiators, mediators, any arbitrators under any of the Arbitration Clauses and any CPR Arbitration Panel (as defined below) to conduct such negotiations, mediation or arbitration, with the sole purpose of maintaining to the extent reasonable the Commercialization of Sevoflurane and at the same time returning, to the extent reasonable, taking into consideration the nature of a breach by a party to a Sevoflurane Agreement and the impact

thereof on the Original Commercial Relationship, the relationship of the parties in an overall contractual and overall economic sense to the Original Commercial Relationship. Any negotiators, mediators and CPR Arbitration Panels shall resolve disputes submitted to negotiation, mediation or arbitration hereunder by the exercise of sound and impartial business judgment. Notwith-standing the foregoing: (i) each of Abbott, Central Glass and Maruishi acknowledges that Baxter has not seen, or participated in the negotiation of, the Abbott/Maruishi Agree-ment; (ii) each of Central Glass and Maruishi acknowledges that Baxter has not seen, or participated in the negotiation of the Central Glass/Maruishi Agreement; (iii) each of Baxter and Maruishi acknowledges that Abbott has not seen, or participated in the negotiation of the Baxter/Maruishi Agreement; (iv) each of Central Glass and Maruishi acknowledges that Abbott has not seen, or participated in the negotiation of, Annex I to the Central Glass/Maruishi Agreement, which Annex I contains the terms of the financial arrangement between Central Glass and Maruishi; and (v) the parties hereto hereby agree that this Agreement shall not be interpreted or applied in any negotiation, mediation or arbitration hereunder so as to involve Baxter in the determination of any circumstances under which Abbott, Central Glass or Maruishi manufactures, markets or sells Sevoflurane, except to the extent Baxter's intellectual property rights entitle it to participate.

An "Impairment of the Original Commercial Relationship" shall mean: (a) an alleged breach or termination of one of the Sevoflurane Agreements that results or could reasonably be expected to result in any change or potential change in the Original Commercial Relationship that would: (i) cause a party to pay more to exercise any of its rights under any of the Sevoflurane Agreements than, but for such change, it would otherwise have been required to pay, including, without limitation, the purchase price such party is required to pay for Sevoflurane and/or HFIP; (ii) prevent a party from

exercising any of the rights licensed or sublicensed to it under any of the Sevoflurane Agreements or performing any of its obligations undertaken under any of the Sevoflurane Agreements; (iii) reduce the amount a party would but for such change otherwise receive under any Sevoflurane Agreement; (iv) prevent a party from receiving its full rights or full commercial benefits under any of the Sevoflurane Agree-ments; (v) prevent or impair the Commercialization of Sevoflurane; or (vi) otherwise impair the Original Commercial Relationship in such a way that it could be reasonably concluded that any one of the parties would not have entered into the Sevoflurane Agreement on the original terms and conditions actually set forth in the Sevoflurane Agreements if such change were in effect at the time of entering into the Sevoflurane Agreement, or (b) any Arbitral Resolution (as defined below) subjecting any party hereto to a result that materially conflicts with the results of any other Arbitral Resolution.

2. *Performance under the Sevoflurane Agreements.*

2.1 Performance *under the Sevoflurane Agreements.* If any party hereto shall have invoked the dispute resolution provisions of this Agreement pursuant to Section 5 hereof, then during the interim period while the matter that has given rise to such invocation is being resolved pursuant to Section 5, 6 or 7 hereof: (i) each party hereto shall, so long as such party continues to perform in good faith all of its obligations under the Sevoflurane Agreements in a reasonable fashion, be entitled to receive all of its rights and benefits under such Sevoflurane Agreements, including, without limitation, the rights licensed or sublicensed to it under any Sevoflurane Agreement and the right to manufacture and sell or purchase Sevoflurane and HFIP at the prices set forth in such Sevoflurane Agreement; and (ii) each party to a Sevoflurane Agreement that continues to receive substantially all of the benefits to which it is entitled under any Sevoflurane

Agreement shall, so long as the other party to such Sevoflurane Agreement continues to perform in good faith substantially all of its obligations in a reasonable fashion, shall continue to perform its obligations under such Sevoflurane Agreement in accordance with the terms thereof.

2.2 *Direct* Payments *by Abbott to Baxter or Central Glass.* Subject to Section 2.3 hereof, during the interim period while any disputes are being resolved under this Agreement, Abbott will continue to make payments to Maruishi as contemplated under the Abbott/Maruishi Agreement (or Central Glass pursuant to Section 14.7 thereof), Maruishi will continue to make payments to Central Glass as contemplated under the Central Glass/Maruishi Agreement and to Baxter as contemplated under the Baxter/Maruishi Agreement, and Central Glass, if it has exercised the License Option (as defined in the Central Glass/Maruishi Agreement), will continue to make payments to Maruishi as contemplated under the Central Glass/Maruishi Agreement. If either of Baxter or Central Glass concludes in good faith that it is not receiving in full the payments to which it is entitled under the Sevoflurane Agreement with Maruishi to which it is a party, and Baxter or Central Glass, as the case may be, has notified the other parties to this Agreement in accordance with Section 4 hereof that a dispute exists with Maruishi, Baxter or Central Glass, as the case may be, may by notice to Abbott specifying the amount of the direct payment (a "Direct Payment Notice") direct Abbott to pay the payments to which such party is entitled under the respective Sevoflurane Agreement directly to Baxter or Central Glass, as the case may be, and not to Maruishi. Each Direct Payment Notice shall include an explanation of such conclusion. At the time of providing a Direct Payment Notice to Abbott, such notifying party shall provide a copy thereof to the other parties hereto. Notwithstanding actual receipt of any Direct Payment Notice by Abbott, Abbott shall pay to Maruishi in accordance with the terms of the Abbott/Maruishi Agreement (or Central Glass

pursuant to Section 14.7 thereof) such amount that it would otherwise be obligated to pay Maruishi pursuant to the Abbott/Maruishi Agreement (or Central Glass pursuant to Section 14.7 thereof), less the amount set forth in such Direct Payment Notice, which shall be paid as described below. Promptly after actual receipt of a Direct Payment Notice, Abbott shall confirm in writing with all of the other parties that all of them have received a copy thereof and such other parties shall confirm such receipt prior to the end of such fifteen (15) day period; it being understood that failure to confirm such receipt within such fifteen (15) day period shall be deemed to constitute receipt and consent. If within fifteen (15) days of the date of such Direct Payment Notice Abbott has not been instructed by Maruishi not to comply with the terms of such Direct Payment Notice, and if Abbott has complied with the terms of the immediately preceding sentence, then Abbott shall comply with the direction set forth in such Direct Payment Notice and Maruishi, Central Glass and Baxter shall make no claim against Abbott with respect to such payment and shall continue to perform their respective obligations under the Sevoflurane Agreements. If within fifteen (15) days of the date of such Direct Payment Notice, Maruishi does instruct Abbott not to comply with the terms thereof, then the matter giving rise to such disagreement over payment shall be submitted to arbitration immediately in accordance with Section 7.1 hereof, Abbott shall deposit in an escrow account the amount of the direct payment set forth in such Direct Payment Notice and the proceeds of such escrow account shall be distributed in accordance with the decision of the CPR Arbitral Panel or as otherwise agreed between Baxter, Maruishi and Central Glass. After submission of such a dispute to arbitration, subsequent payments by Abbott of amounts similarly in dispute shall also at the good faith direction of the party giving the Direct Payment Notice be paid into such escrow account. The parties hereby instruct the CPR Arbitral Panel

that in the event that a matter is submitted to arbitration pursuant to this Section 2.2, the CPR Arbitral Panel shall conduct such proceedings on an expedited basis and within thirty (30) days after the empaneling of the CPR Arbitral Panel and thereafter on a monthly basis so long as such arbitration continues shall disburse from the escrow account to Central Glass, Baxter or Maruishi as the CPR Arbitral Panel determines appropriate such amount as is necessary to maintain to the extent reasonable the Commercialization of Sevoflurane taking into account the nature and extent of the Impairment of the Original Commercial Relationship. The parties hereto agree that Abbott may make any payments it may otherwise have been obligated to make during the time period described in this Section 2.2 that are not the subject of the Direct Payment Notice as specified in the Abbott/ Maruishi Agreement.

2.3 *Central Glass License Option.* The parties hereto hereby agree that during the interim period while any disputes are being resolved under this Agreement as an alternative to the potential direct payment of monies from Abbott to Central Glass pursuant to Section 2.2 hereof, Maruishi hereby grants Central Glass the option, and Maruishi agrees that Central Glass may obtain the right to an exclusive, non-transferable sublicense, with no right to sublicense, under the Baxter Patents, the Baxter Japanese Patents and the Baxter Technical Information and Know-How and the related Improvements (as such capitalized terms are defined in the Central Glass/Maruishi Agreement) to make Sevoflurane in Japan and in the Territory (as defined in the Central Glass/Maruishi Agreement) and sell such Sevoflurane and, in certain circumstances pursuant to Section 2.2, Section 9.3 or Article 20 of the Abbott/Maruishi Agreement, the right to sell HFIP, directly to Abbott and, upon exercise of such right, the license granted to Central Glass pursuant to Subsection 14.1(a) of the Central Glass/Maruishi Agreement will automatically be modified to grant Central Glass such right (the "License

Option"). Subject to the next sentence, Central Glass may only exercise such License Option where Maruishi has failed to make payments due to Central Glass pursuant to Section 5.2 of the Central Glass/Maruishi Agreement on a timely basis and any Option Triggering Event (as defined below) exists. Central Glass agrees to give Maruishi and Abbott thirty (30) days' advance written notice prior to exercising its License Option and if Maruishi pays all delinquent amounts to Central Glass and remedies any and all Option Triggering Events during such thirty (30) day period, then Central Glass may not exercise its License Option. In the event Central Glass exercises its License Option and sells Sevoflurane or HFIP, as the case may be, directly to Abbott, Abbott will pay Central Glass directly in accordance with Section 5.2 of the Abbott/Maruishi Agreement and such exercise will not change the amounts which Abbott would otherwise be required to pay for the purchase of Sevoflurane or HFIP pursuant to the terms of the Abbott/Maruishi Agreement. Central Glass will pay to Maruishi the amount which Maruishi is entitled to receive from such Sevoflurane or HFIP sales to Abbott pursuant to Annex I of the Central Glass/ Maruishi Agreement within the earlier of: (i) ten (10) days after receipt of payment for such Sevoflurane or HFIP by Central Glass from Abbott; or (ii) ninety (90) days after the date of the bill of lading reflecting delivery of such Sevoflurane or HFIP to Abbott FOB Tokyo, by wire transfer to the bank account designated by Maruishi. Central Glass's License Option will terminate immediately upon payment of all amounts in default to Central Glass pursuant to Section 5.2 of the Central Glass/Maruishi Agreement and the end of all Option Triggering Events, at which time Maruishi and Central Glass will give joint notice to Abbott thereof, and at such time the license granted in Subsection 14.1(a) of the Central Glass/Maruishi Agreement will revert to the terms provided therein and Central Glass will sell Sevoflurane and HFIP exclusively to Maruishi in accordance with the other

terms of the Central Glass/Maruishi Agreement. The term "Option Triggering Event" as used herein means: (i) failure by Maruishi to pay any of its other material indebtedness in accordance with the terms of the relevant agreements evidencing such indebtedness where such failure to pay continues for a period of at least sixty (60) days; (ii) the stated maturity of any borrowing or guarantee obligation of Maruishi has been accelerated due to any default by Maruishi in respect thereof; or (iii) any clearinghouse taxes procedure for suspension of Maruishi's transactions with banks and similar institutions in accordance with the rules of such clearinghouse.

3. *Arbitration under the Sevoflurane Agreements*. In the event that any party to any of the Sevoflurane Agreements submits a dispute arising out of or relating to such Sevoflurane Agreement or the breach, termination or validity thereof including, without limitation, the determination of the arbitrability of such a dispute (a "Disputed Matter") to arbitration in accordance with such Sevoflurane Agreement, then, subject to Section 2.1 hereof and the rights of any party hereto to invoke the dispute resolution provisions hereof in accordance with Section 5 hereof, during the course of such arbitration each of the parties hereto covenants not to bring any action, whether at law or in equity, with any court, arbitral body or other tribunal, including, without limitation, any of the arbitral bodies referred to in any of the Arbitration Clauses, against any other party relating to a Disputed Matter other than such actions as are permitted under the Arbitration Clause in the disputed Sevoflurane Agreement. Subject to Section 2.1 hereof, during the interim period while any disputes are being resolved under this Agreement each of the parties hereto covenants not to bring any action, whether at law or in equity, with any court, arbitral body or other tribunal, against any other party relating to a Disputed Matter other than such actions as are otherwise permitted hereunder.

4. *Notice Concerning Potential Impairment of the Original Economic Relationship.* In the event that: (a) a party becomes aware of an issue that may give rise to a right of termination under any Sevoflurane Agreement; (b) a party determines to send a notice terminating a Sevoflurane Agreement; (c) a Disputed Matter has been discussed and not resolved between the responsible executives of the parties to a Sevoflurane Agreement in accordance with a provision, if any, of the Arbitration Clause thereof requiring such a meeting before the Disputed Matter is submitted to arbitration; or (d) a party determines to submit a Disputed Matter to arbitration in accordance with an Arbitration Clause; then with respect to clauses (a), (b) and (d) above, such party, and with respect to clause (c) above, both of the parties to the relevant Sevoflurane Agreement, shall give notice (which notice in the case of clause (b) above shall be given at least thirty (30) days prior to giving any termination notice and in the case of clause (d) above shall be given at least thirty (30) days prior to submitting the Disputed Matter to arbitration) to the other parties hereto of such issue, determination or event with an explanation thereof and of the relevant Disputed Matter and whether it in good faith believes that such termination or Disputed Matter or the resolution thereof will result in an Impairment of the Original Commercial Relationship and a summary of the evidence and arguments supporting such belief.

5. *Negotiation.* Any party (a "Noticing Party") which is a party to a dispute referred to in Section 3 hereof or which receives a notice pursuant to Section 4 hereof, which reasonably concludes in good faith that, as a result of such dispute, a potential Impairment of the Original Commercial Relationship exists or that the resolution of any Disputed Matter pursuant to the decision of the arbitrators in any arbitration described in Section 3 hereof or any settlement of such Disputed Matter by the parties to such arbitration (any such resolution or settlement being hereinafter referred to as an "Arbitration Resolution"), would, if enforced, result in, or

has already resulted in, an Impairment of the Original Commercial Relationship, may give the other parties written notice thereof. Once a party shall have given such a notice with respect to an arbitral proceeding under any Arbitration Clause, such arbitral proceeding shall be suspended and the matter resolved as set forth herein. Within thirty (30) days after receipt of such notice, each of the receiving parties shall submit to the other parties hereto a written response. The notice and responses shall include: (i) a statement of each party's position, including its proposal for resolving the Disputed Matter, amending the Arbitration Resolution or otherwise adjusting the relationship of the parties (to the extent known to such party) in order to maintain, to the extent reasonable, the Commercialization of Sevoflurane and at the same time to return, to the extent reasonable, taking into consideration the nature of the breach by a party to a Sevoflurane Agreement and the impact thereof on the Original Commercial Relationship, the relationship of the parties in an overall contractual and overall economic sense to the Original Commercial Relationship, by preventing and/or curing the Impairment of Original Commercial Relationship, and a summary of the evidence and arguments supporting its position, and (ii) the name and title of a senior executive who has authority to settle the matter, who does not have direct day-to-day responsibility for administration of any Sevoflurane Agreement and who will represent that party. The parties will attempt in good faith to resolve their differences promptly by negotiations between such senior executives who shall meet at a mutually acceptable time and place within ten (10) days after the date of the last of the written responses to be delivered as described above and thereafter as often as they reasonably deem necessary to exchange relevant information and to attempt to resolve the matter; *provided*, *however*, that a party that is not a party to the Sevoflurane Agreement that is proposed to be terminated, if any, is not a party to the Sevoflurane Agreement under

which such Disputed Matter arose, if any, is not affected by the Arbitration Resolution, if any, and is not affected by the potential Impairment of the Original Commercial Relationship, is not required to participate in such negotiations, attend such meetings, or participate in the subsequent mediation under Section 6 hereof or arbitration under Section 7 hereof, if any, but shall offer such assistance as may be reasonable in helping the other parties to resolve the Disputed Matter.

6. *Mediation.* If a matter has not been resolved within sixty (60) days of the Noticing Party's notice described in Section 5 hereof, then the parties shall initiate mediation of the matter in accordance with the Center for Public Resources Model Procedure for Mediation of Business Disputes.

7. *Arbitraiton.*

7.1 *Submission of Dispute to Arbitration.* Any matter that has been submitted to arbitration pursuant to Section 2.2 hereof and any matter being mediated pursuant to Section 6 hereof that has not been resolved pursuant to such mediation procedure within ninety (90) days of the initiation of such mediation procedure shall be settled by arbitration on accordance with the Center for Public Resources Rules for Non-Administered Arbitration of International Disputes (the "CPR Rules") by three arbitrators (the "CPR Arbitral Panel") who shall be appointed by the Center for Public Resources from its Panels of Distinguished Neutrals in accordance with Rule 6 of the CPR Rules. One such arbitrator shall be a Japanese national fluent in the English language, one shall be a U.S. national, and the third shall be a person fluent in English and a national of a country other than Japan or the U.S. In resolving a dispute, the CPR Arbitral Panel shall apply the substantive law, if any, set forth in the Sevoflurane Agreement under which such dispute arose as the governing law of such Sevoflurane Agreement and, if none is specified, the CPR Arbitral Panel shall apply the substantive law of Japan or the State of Illinois, whichever the CPR Arbitral

Panel determines appropriate. The arbitration shall be conducted in the English language (with iterative Japanese translation if either Central Glass or Maruishi is a party to such arbitration) and shall be held at a neutral site designated by the CPR Arbitral Panel. The neutral organization designated to perform the functions specified in Rule 6 and Rules 7.7(b), 7.8 and 7.9 of the CPR Rules shall be the Center for Public Resources.

7.2 *Suspension or Modification of Arbitral Resolutions; No Punitive Damages*. In addition to the rights granted to the CPR Arbitral Panel pursuant to the CPR Rules, the CPR Arbitral Panel shall have the right, notwithstanding the provisions of any Arbitration Clause or the rules of any arbitral body that has conducted any arbitration resulting in an Arbitral Resolution, to suspend the operation of any arbitral proceedings being conducted pursuant to an Arbitration Clause and to suspend the enforcement or modify the terms of any Arbitration Resolution relating to a dispute that has been submitted to the arbitrators for resolution pursuant to this Section 7. The CPR Arbitral Panel is not empowered to award damages, punitive damages or other damages in excess of actual damages, but is empowered to adjust the amount of payments made by any party during the period that Section 2 hereof was in effect including a refund of all or any portion of such payment with interest calculated in accordance with Section 7.4 hereof to reflect the actual benefits received and the actual obligations performed.

7.3 *Provisional Relief and Injunctive Relief.* Any party may file an application in any proper court for a provisional remedy in connection with an arbitrable controversy hereunder, but only upon the ground that the award to which the applicant may be entitled may be rendered ineffectual without provisional relief. Despite such action, the parties will continue to participate in good faith in the procedures

specified in this Section 7. The CPR Arbitral Panel shall have the power to give injunctive relief.

7.4 *Awards in Dollars or Yen.* Any monetary awards made by the CPR Arbitral Panel, other than in a Disputed Matter involving only Maruishi and Central Glass, shall be made and shall be payable in U.S. dollars through a bank in the United States and shall be subject to any tax or other deduction required by applicable law. Monetary awards between Maruishi and Central Glass only shall be made and shall be payable in Japanese yen through a bank in Japan and shall be subject to any tax or other deduction required by applicable law. Monetary awards shall include interest from the date of breach or other violation of the relevant Sevoflurane Agreement to the date when the award is paid in full. The interest rate or rates applied to dollar amounts during such period shall be the prime commercial lending rate announced from time to time by Citibank, N.A. at its principal office in New York City plus 2% and the interest rate or rates applied during such period to yen amounts shall be the prime commercial lending rate announced from time to time by The Dai-Ichi Kangye Bank, Limited at its principal office in Tokyo plus 2%.

7.5 *Enforcement.* The award or order of the CPR Arbitral Panel will be the sole and exclusive remedy between the parties hereto regarding any and all claims and counterclaims with respect to the Disputed Matter. An award or order rendered in connection with an arbitration pursuant to this Section 7 shall be final and binding upon the parties, and any judgment upon such an award may be entered and enforced in any court of competent jurisdiction. The parties hereby waive all jurisdictional defenses in connection with any arbitration hereunder or the enforcement of an order or award rendered pursuant thereto (assuming that the terms and conditions of this arbitration clause have been complied with) and defenses based on the general invalidity of the underlying

Sevoflurane Agreement or this arbitration clause and hereby waive defenses arising under Articles 801(4)-(5) of the Japanese Code of Civil Procedure. With respect to any award or order issued by the CPR Arbitral Panel pursuant to this Agreement, the parties expressly agree and consent (x) to the bringing of an action by one party against the other parties in the federal courts of Illinois or any Japanese court to enforce and confirm such award or order; (y) that such award or order shall be conclusive proof of the validity of the determination(s) of the CPR Arbitral Panel underlying such award or order; and (z) that any federal court sitting in Illinois or any Japanese court may enter judgment upon and enforce such award or order, whether pursuant to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958, the United States Arbitration Act, 9 U.S.C. §§ 1-16, or otherwise.

7.6 *Cost of CPR Arbitral Panel and Translation.* All fees, costs and expenses of the CPR Arbitral Panel shall be shared equally by the parties to any arbitration. The cost of translation of arbitral proceedings into Japanese shall be shared equally by Maruishi and Central Glass if they both participate in such arbitration; otherwise, only the party so participating shall bear all such costs.

8. *MISCELLANEOUS*

8.1 *Effectiveness.* This Agreement will come into effect upon the first date (the "Effective Date") on which all of the following documents become fully executed: (i) this Agreement; (ii) the Abbott/Maruishi Agreement; (iii) the Baxter/Maruishi Agreement; (iv) the Central Glass/Maruishi Agreement; and (v) the Central Glass/Abbott Side Letter.

8.2 *Governing Law.* The validity, interpretation, enforceability and performance of this Agreement shall be governed by and construed in accordance with the laws of the State of Illinois.

8.3 *Severability.* If any provision of this Agreement is declared invalid or unenforceable by any lawful tribunal, then it will be adjusted to conform to legal requirements of that tribunal and that modification will automatically become a part of this Agreement. If no adjustment can be made, the provision will be deleted as though never included in this Agreement and the remaining provisions of this Agreement will remain in full force and effect unless such invalidity or unenforceability causes substantial deviation from the underlying intent of the parties expressed in this Agreement, in which case the parties will replace the invalid or unenforceable provision with a valid or enforceable provision which corresponds as far as possible to the spirit and purpose of the invalid or unenforceable provision.

8.4 *Non-Waiver.* All rights and remedies conferred under this Agreement or by any other instrument or law will be cumulative, and may be exercised singularly or concurrently. Failure by any party to enforce any provision will not be deemed a waiver of future enforcement of that or any other provision.

8.5 *Notice.* All notices required or permitted under this Agreement shall be in writing and shall be deemed to have been given upon personal delivery or, except for a Direct Payment Notice to Abbott which must actually be received by Abbott, upon the expiration of six (6) days following deposit in mail, registered, first class, with postage prepaid or by courier. Notices may also be given by telefax, and will be effective upon receipt of confirmation of receipt or, except for a Direct Payment Notice to Abbott which must actually be received by Abbott, upon the expiration of two (2) days

following transmission. The addresses of the parties (until written notice of change shall have been given) will be as follows:

If to Abbott:

Abbott Laboratories
One Abbott Park Road
Abbott Park, IL 60064-3500
United States of America
Attn: President, Abbott
International Division
Telefax: 1-708-938-8325
Attn: President, Hospital
Products Division
Telefax: 1-708-937-0805

If to Baxter:

Baxter International Inc.
One Baxter Parkway
Deerfield, IL 60015
United States of America
Attn: General Counsel
Telefax: 1-708-948-3429

If to Central Glass:

Central Glass Co., Ltd.
Kowa-Mitztsubashi Bldg.
7-1, Kanda-Nishikicho
3-chome
Chiyoda-ku
Tokyo 101
Japan
Attn: General Manager,
Fine Chemicals Department
Telefax: 81-3-3293-2145

If to Maruishi:

Maruishi Pharmaecutical
Co., Ltd.
3-5, Fushimi-machi
2-chome
Chuo-ku
Osaka 541
Japan
Attn: President
Telefax: 81-6-231-6696

8.6 *Amendment.* This Agreement may be modified, changed or amended only in a writing signed by each of the parties.

8.7 *Assignment.* No party may transfer or assign this Agreement or any of its rights or obligations hereunder, directly, indirectly, or in connection with any change in control (defined as the acquisition of more than fifty percent (50%) of the voting shares of the party or of more than fifty

percent (50%) of the assets of the party) by any person, entity or group (other than existing affiliates of the party) in a single transaction or series of transactions), without obtaining prior written approval from the other parties hereto; *provided, however*, that upon the assignment of any Sevoflurane Agreement by any party in accordance with the terms thereof, such party shall also assign and delegate its rights and obligations under this Agreement to the assignee of such Sevoflurane Agreement. In the event of any permitted assignment, this Agreement will bind and inure to the benefit of the assignee.

8.8 *English Language.* The English language version of this Agreement will be controlling in all respects, notwithstanding any translation made of this Agreement for any purpose whatsoever.

8.9 *Headings and Recitals.* The headings and recitals appearing in this Agreement have been used for reference purposes only and will not affect the interpretation or enforcement of this Agreement.

8.10 *Counterparts and Facsimiles.* This Agreement may be executed in four (4) counterparts, in which case each counterpart will be deemed an original, but all of which, taken together, will constitute the same Agreement. Execution and delivery of this Agreement by exchange of facsimile copies bearing the facsimile signature of a party hereto shall constitute a valid and binding execution and delivery of this agreement. Such facsimile copies shall constitute enforceable original documents.

IN WITNESS WHEREOF, the parties hereto have caused their duly authorized representatives to execute this Agreement as of the Effective Date.

ABBOTT LABORATORIES

By:/s/ Thomas R. Hodgson
Thomas R. Hodgson
President

Date: 9/18/92

BAXTER INTERNATIONAL INC.

By: /s/ [illegible]
Title: [illegible]

Date: 9/18/92

CENTRAL GLASS CO., LTD.

By: /s/ H. Okazaki
Hirotaro Okazaki
President

Date: Sept. 18, 1992

MARUISHI PHARMACEUTICAL CO., LTD.

By: /s/ Nobuyuki Inoue
Nobuyuki Inoue
President

Date: 18 Sept. '92

Supreme Court, U.S.
FILED
SEP 8 2003
OFFICE OF THE CLERK

No. 03-59

IN THE

Supreme Court of the United States

BAXTER INTERNATIONAL, INCORPORATED,

Petitioner,

v.

ABBOTT LABORATORIES,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals erred in ruling that petitioner was not entitled to relitigate in federal court an issue of federal antitrust law that petitioner submitted for resolution to an arbitration tribunal and which that tribunal then decided.

CORPORATE DISCLOSURE STATEMENT

Respondent Abbott Laboratories has no parent company, and no publicly held corporation owns 10% or more of respondent's stock.

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BAXTER INTERNATIONAL, INCORPORATED,

Petitioner,

v.

ABBOTT LABORATORIES,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF IN OPPOSITION

STATEMENT

Petitioner Baxter International, Incorporated ("Baxter") submitted for an arbitration tribunal's resolution an affirmative defense (to a breach of contract claim) that Baxter contended arose under federal antitrust law, which both the arbitration tribunal and the district court below concluded lacked any merit. The court of appeals affirmed on the ground

that petitioner should not be allowed to relitigate in federal court an issue of federal law that petitioner submitted to the arbitration tribunal and that the tribunal actually decided. The court of appeals reasoned that permitting relitigation in such an instance would violate the parties' agreement to arbitrate and the arbitrators' determination of such issues. Seeing no violation of the antitrust laws, the court of appeals further found that enforcement of the resulting arbitration award is not contrary to public policy.

Because the court of appeals' decision is correct, is entirely in accord with this Court's precedent, and does not conflict with any decision of any other federal court of appeals, further review is not warranted.

A. The Sevoflurane Agreements

Baxter developed sevoflurane, an inhalation anesthetic, as well as a one-step process for its creation. Baxter obtained both a product patent for sevoflurane, since expired, and process patents for the one-step process, the last of which is due to expire in December 2005. Pet. App. 1a, 19a-20a.

In 1998, Baxter decided not to pursue commercialization of the product, so it granted to Maruishi Pharmaceutical Co., Ltd. ("Maruishi"), a Japanese company, an exclusive worldwide license to practice Baxter's sevoflurane patented process. Maruishi successfully developed sevoflurane in Japan, but did not have the capability to do so elsewhere. It sought out, with Baxter's consent, other potential sublicensees to commercialize the product outside Japan. Maruishi, again with Baxter's consent, determined that respondent Abbott Laboratories ("Abbott") presented the best chance for expanded commercialization of the product. Pet. App. 1a-2a, 19a-20a.

To that end, Baxter, Maruishi, Abbott, and another Japanese company, Central Glass Co., Ltd. ("Central Glass"), entered into a series of detailed agreements in 1992. These agreements provided that Baxter would license its sevoflurane patents to Maruishi, Maruishi would sublicense these patents to Abbott, Central Glass would manufacture sevoflurane for exclusive sale to Maruishi for resale exclusively to Abbott, Abbott would seek to commercialize sevoflurane in the United States (and elsewhere), and Abbott would pay royalties on sales of sevoflurane (through Maruishi) to Baxter. At the same time, the parties entered into a Dispute Resolution Agreement, which included detailed provisions for the resolution of disputes under the other agreements (and separately prohibited impairment of the Original Commercial Relationship among the parties), culminating in "final and binding" arbitration. Pet. App. 2a, 23a-24a.

Abbott began the task of gaining FDA approval for sevoflurane in 1992, but approval was not granted until 1995. After FDA approval was obtained, Abbott began to commercialize sevoflurane in the United States. This product had not previously been available to those in need of anesthetics in the United States. Between 1992 and 2000, Abbott expended $1.434 billion to commercialize sevoflurane. Baxter has received tens of millions of dollars in royalties from Abbott on sales of sevoflurane. Pet. App. 2a-3a, 26a.

The four-way agreements among the parties functioned well until 1998, when Baxter acquired, for approximately $94 million, certain assets of a company (Ohmeda) that had developed a three-step process for making a generic sevoflurane. Baxter did not notify the other parties of its intent to acquire Ohmeda. Thereafter, Baxter announced its plans to compete with its own licensee and sublicensee by selling Ohmeda generic sevoflurane in the United States. Had Baxter not acquired

Ohmeda, there would be no arbitration or the resultant appeals since Ohmeda was otherwise prepared to seek FDA approval of its generic sevoflurane and had constructed its own manufacturing plant in Puerto Rico. Abbott demanded binding arbitration, pursuant to the Dispute Resolution Agreement, of its claim that Baxter would violate both the Baxter/Maruishi Agreement and the Dispute Resolution Agreement if it sold generic sevoflurane in competition with its own sublicensee before the December 2005 expiration of the 1992 sevoflurane agreements. Pet. App. 2a-3a, 26a-27a.

B. Proceedings Below

1. The arbitration tribunal ordered Baxter not to sell or market sevoflurane in the territory defined in the Maruishi/Abbott Agreement until the expiration of that agreement in December 2005. Pet. App. 43a-68a. The tribunal concluded that Baxter's action constituted both a breach of its duty of good faith under the Baxter/Maruishi Agreement (under which Abbott had a right to sue as a third party beneficiary) and an impairment of the Original Commercial Relationship among the parties under the Dispute Resolution Agreement, entitling Abbott to relief under both Agreements.[1] *Id.* at 65a. Baxter does not appeal from either of those rulings here.

During the arbitration proceedings, Baxter defended against Abbott's claim by, among other things, presenting

1. Petitioner incorrectly asserts (Pet. 7 n.1) that the court of appeals erred "when it stated Baxter's sale of generic sevoflurane would violate the Baxter-Maruishi license." According to petitioner, the arbitration tribunal did not find a breach of that licensing agreement, but instead relied exclusively on the Dispute Resolution Agreement. Petitioner is in error. As the award makes plain, the tribunal concluded that "the obligation of good faith under Illinois law in this case establishes an independent cause of action under the Baxter/Maruishi Agreement" and that Baxter breached that duty (along with the Original Commercial Relationship). Pet. App. 65a.

affirmative defenses that Abbott's requested relief would result in a violation of section 1 of the Sherman Act, as well as a consent decree between the FTC and Abbott. *Id.* at 66a. The tribunal concluded that "no illegality results from the interpretation of the Sevoflurane Agreements in this award." *Id.* The tribunal found that Baxter's antitrust issues "do not arise from those Agreements themselves" but are instead "a result of Baxter's acquisition of Ohmeda . . . which removed from the Sevoflurane market the very type of independent generic competitor foreseen by the Parties in 1992." *Id.* at 67a.[2]

2. The district court confirmed the arbitration award. Pet. App. 19a-42a. The court rejected Baxter's contention that the arbitration "tribunal's interpretation of the Sevoflurane Agreements is a market allocation agreement and thus is a *per se* violation of section 1 of the Sherman Act." *Id.* at 31a. The court agreed with the tribunal that Baxter's claim lacked merit because "the only adverse impact on competition was due to the actions of Baxter and not the tribunal's interpretation of the Sevoflurane Agreements." *Id.* at 34a.

The court found that "there is no evidence in the record as to the parties' intent to divide the market or minimize competition" and that "[t]he record is silent with respect to Abbott's harm to generic competition." *Id.* at 34a. "There were no facts presented to the arbitrators to support any type of market allocation." *Id.* at 35a. The court stressed that "the injury now alleged by Baxter is not your typical type of antitrust injury" because "Baxter, who profits tremendously

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2. One arbitrator dissented from the award on grounds unrelated to Baxter's affirmative defenses. Pet. App. 69a-91a.

from its contractual arrangement with Abbott, wants to increase its profits by introducing generic sevoflurane, thus establishing its presence in the generic submarket as well as the existing sevoflurane market which Baxter currently profits from." *Id.* at 34a.

The district court also rejected Baxter's alternative contentions that the arbitration tribunal's decision created an unlawful "ancillary covenant not to compete" or a Sherman Act Section 1 violation "under a rule of reason analysis." Pet. App. 35a-38a. With regard to the former, the court found no such unlawful covenant because "Baxter is free to sell other inhaled anesthetics and admits to the sale," "there is no allegation that the agreement between Abbott and Baxter was created to raise the price of sevoflurane," and "Baxter has not established that generic competition is not still possible." *Id.* at 36a, 37a. With regard to the last, the court concluded that, judging the effects of the licensing arrangement as of the time the contract was entered into, "the licensing arrangement was pro-competitive." *Id.* at 39a.[3]

3. The court of appeals affirmed. Pet. App. 1a-7a. The court held that Baxter is not "entitled to reargue an issue that was resolved by the arbitral tribunal" because "a mistake of law is not a ground on which to set aside an award." *Id.* at 4a. Relying on this Court's decision in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985) "that international arbitration of antitrust disputes is appropriate[,]" the appellate tribunal reasoned that "*Mitsubishi* did not contemplate that, once arbitration was

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3. The district court also rejected Baxter's claims that the tribunal's award required Abbott to violate a FTC consent decree or contravened Illinois public policy. Pet. App. 39a-42a.

over, the federal courts would throw the result in the waste basket and litigate the antitrust issues anew." Pet. App. 5a.

The court did not question Baxter's assertion "that arbitrators are not allowed to command the parties to violate rules of positive law[,]" explaining instead that "*whether* the tribunal's construction of the Baxter-Maruishi agreement has that effect was a question put to, and resolved by, the arbitrators. They answered no, and as between Baxter and Abbott their answer is conclusive." Pet. App. 5a-6a (emphasis in original).

Finally, the court separately set forth several reasons why treating Baxter as bound by the arbitration tribunal's conclusion does not violate "public policy." First, the appellate court recognized that the exclusivity rule of the licensing agreement "was a lawful ancillary agreement designed to induce Maruishi and its sublicensees to make the investments needed to bring the new drug to market." Pet. App. 6a-7a. Second, the tribunal's award "does not condemn the public to tolerate a monopoly" because, if the arrangement "really does offend the Sherman Act, then the United States, the FTC, or any other purchaser of sevoflurane is free to sue and obtain relief." *Id.* at 6a. The arbitration award bars only Baxter from relitigating the issue, and "Baxter, as a producer, is a poor champion of consumers." *Id.* at 6a. Third, "if there is an antitrust problem, it lies in the acquisition — and the remedy would be [Baxter's] divestiture of the Ohmeda process patent . . . Baxter, which can solve unilaterally any antitrust problem, is in no position to insist that the burden of the solution fall on Abbott by depriving it of the benefit of the exclusive Baxter-Maruishi license." *Id.* at 7a.[4]

4. One judge dissented from the court of appeals' ruling (Pet. App. 8a-18a), and three judges dissented from the court's denial of rehearing *en banc*. *Id.* at 92a-94a.

REASONS FOR DENYING THE PETITION

Petitioner misstates the ruling of the court of appeals below. The court of appeals' ruling was entirely grounded in the particular facts of this case (factual determinations that were both fatal to Baxter's theory and exclusively within the province of the arbitral panel) and correct.

Contrary to the premise underlying petitioner's "Question Presented" (Pet. i), the court of appeals did *not* rule that "an arbitration panel may shield its award from court review for compliance with public policy." The court below did *not* hold that courts are wholly powerless to refuse to enforce arbitration rulings on the ground that they are void for public policy.

The court of appeals instead based its ruling that the particular arbitration award challenged in this case should not be disturbed upon the presence of at least three specific circumstances: (1) the arbitration tribunal plainly had jurisdiction to address petitioner's antitrust affirmative defense, and petitioner expressly invited the tribunal to do so; (2) the arbitration tribunal actually decided that legal issue (which, by definition, was embedded in the tribunal's findings of fact), and petitioner is not entitled to relitigate an affirmative defense that was resolved by the arbitration tribunal, because a mistake of law is not a ground on which to set aside an arbitration award; and (3) the case presents no judicial occasion to refuse to enforce the arbitration award on "public policy" grounds because no antitrust problem appeared from the record.

No further review is warranted. The court of appeals' decision is correct, is entirely consistent with decisions of this Court, and does not conflict with the rulings of any other federal circuit. The petition, accordingly, should be denied.

1. The court of appeals correctly declined to allow petitioner to relitigate the antitrust affirmative defense, which the district court also rejected on the merits. The arbitration tribunal considered and addressed the antitrust defense that petitioner then sought to raise anew in court, and indeed the tribunal did so at petitioner's own express invitation. In any event, legal errors in the determination of an arbitration tribunal do not provide a ground upon which to set aside an award.

As this Court previously recognized, the Convention on the Recognition and Enforcement of Foreign Arbitration Awards, 21 U.S.T. 2517, T.I.A.S. No. 6997, which is the subject of domestic implementing legislation (*see* 9 U.S.C. §§ 201-208), expressly sets forth the grounds for refusing to enforce an international arbitration award. Not surprisingly, a legal error is not one of them. Arbitrators have "free rein to decide the law as well as the facts and are not subject to appellate review." *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145, 149 (1968); *see United Paperworkers Int'l Union, AFL-CIO v. Misco, Inc.*, 484 U.S. 29, 37-38 (1987). "[P]lenary review by a court of the merits would make meaningless the provisions [of the contract] that the arbitrator's decision is final." *United Steelworkers of America v. Enterprise Wheel & Car Corp.*, 363 U.S. 593, 599 (1960). Of course, were the rule otherwise, the principal advantage presented by arbitration — avoidance of the time and expense of protracted judicial proceedings — would be eviscerated.

Nor is there any ground for petitioner's implicit suggestion that antitrust law should be treated differently. This Court has already considered and rejected just that contention. In *Mitsubishi*, the Court "decline[d] to subvert the spirit of the United States' accession to the Convention by recognizing subject-matter exceptions where Congress has not expressly directed the courts to do so." 473 U.S. at 639 n.21.

Finally, petitioner's proffered distinction (Pet. 12) between this arbitration tribunal's *resolution* of an antitrust issue and the arbitration award's *creation* of such an issue is wholly illusory. Here, at petitioner's own invitation, one issue presented to the arbitration tribunal was whether the arbitration award would create an antitrust problem. As the court of appeals explained, "*whether* the tribunal's construction of the Baxter-Maruishi agreement has that effect was put to, and resolved by, the arbitrators. They answered no, and as between Baxter and Abbott their answer is conclusive." Pet. App. 6a (emphasis in original).

2. Contrary to petitioner's claim (Pet. 11-12), the court of appeals below in no manner intimated that federal courts cannot decline to enforce an arbitration award on the ground that it is against public policy. Nor is the effect of the court's ruling that arbitration tribunals may "shield" their awards from such public policy review by simply deciding the public policy issue themselves. Petitioner's accusation (Pet. 19-23) that the court of appeals' ruling "threatens effectively to nullify the public policy exception to enforcement of arbitral awards" is misdirected.

Petitioner falsely equates a court's properly declining to revisit a legal issue resolved by the arbitration tribunal with

a court's improperly eschewing its residual judicial authority to refuse to enforce an arbitration award in those extreme circumstances where the award's enforcement would offend public policy. The court of appeals distinguished between the two judicial functions in this case and addressed each in a wholly appropriate fashion.

The appellate court considered whether it had the authority to relitigate an issue of federal antitrust law that the arbitration tribunal had, at petitioner's own invitation, actually decided. The court correctly ruled that it had no such authority. Pet. App. 4a-6a. The appellate court also considered whether enforcement of the arbitration award would lead to a violation of law and concluded that it would not. Pet. App. 6a-7a.

The court of appeals dismissed petitioner's contention that the arbitral award required the parties to violate the antitrust laws, stating that the exclusivity rule of the licensing agreement "was a lawful ancillary agreement" designed to induce investments in a new drug product. Pet. App. 6a-7a.[5] The appellate court also determined that, even if there was an antitrust issue, holding that petitioner was bound by the outcome of the arbitration was not unjust, because any such

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5. "The Rule of Reason . . . has been regarded as a standard for testing the enforceability of covenants in restraint of trade which are ancillary to legitimate transactions." *National Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 689 (1978). Courts reviewing arbitral awards for possible violations of public policy defer to the arbitrators' findings of fact. *Misco*, 484 U.S. at 45. Here, the tribunal's factfinding makes clear that the co-terminous non-compete in the licensing agreement does not violate the antitrust laws under the Rule of Reason, even if petitioner could demonstrate the requisite antitrust injury under § 4 of the Clayton Act. *See* Pet. App. 66a-67a.

problem was created by petitioner's acquisition of Ohmeda and, therefore, could be as easily solved unilaterally by petitioner's divestiture of Ohmeda. *Id.* at 7a. The court of appeals concluded that precluding petitioner from challenging the arbitral award as being violative of the antitrust laws "does not condemn the public to tolerate a monopoly," because other private parties or governmental authorities may bring an antitrust enforcement action. *Id.* at 6a. There is simply no merit to petitioner's contention that the court of appeals declined to consider petitioner's public policy argument.

3. Moreover, this case presents none of the sweeping questions of law and public policy implications set forth in the petition. Petitioner's claims of conflicts with this Court's precedent and with other circuits' rulings all lack merit.

For instance, petitioner's reliance on *Mitsubishi* and *Vimar Seguros y Reaseguros, S.A. v. M/V Sky Reefer*, 515 U.S. 528 (1995) is misplaced. As described by the court of appeals in this case, the *Mitsubishi* Court anticipated the circumstances presented here, where the arbitration tribunal resolved a federal antitrust issue. In such circumstances, the federal judicial role is confined "'to ascertain[ing] that the tribunal took cognizance of the antitrust claims and actually decided them.'" Pet. App. 6a, *quoting* 473 U.S. at 638. That is precisely what the court of appeals did in this case. *See* Pet. App. 6a ("Ensuring this is as far as our review legitimately goes."). While *Mitsubishi* and *Vimar* discussed the distinct circumstance, not presented here, of federal judicial review in the event that an arbitral award constituted a waiver of statutory remedies (*see Vimar*, 515 U.S. at 540, *quoting Mitsubishi*, 473 U.S. at 637 n.19), the Court never suggested that federal courts, under the guise of public policy

review, should allow parties to an arbitration to relitigate issues already submitted to and resolved by the arbitration tribunal.

The other cases upon which petitioner relies are inapposite, because in those cases, unlike here, the arbitrators were not authorized to, and did not, decide the issues later presented to the courts. *See, e.g.*, Pet. 14 (analysis of *W.R. Grace & Co. v. United Rubber Workers Local 759*, 461 U.S. 757 (1983)). In those cases, the issue decided in arbitration was whether disciplining an employee violated a "just cause" provision in the labor agreement (see Pet. 17), whereas the issue presented to the court was whether the reinstatement of the disciplined employee would violate a public policy established by statutes or regulations that were separate and distinct from the labor agreement. Here, by contrast, the antitrust defense that petitioner has argued before the courts is the same issue on which petitioner failed to carry the burden of proof before the arbitration tribunal.[6]

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6. Nowhere in *Eastern Associated Coal Corp. v. United Mine Workers of America, Dist. 17*, 531 U.S. 57, 62 (2000) is it even hinted that the arbitrator decided whether the employer's action comported with the federal regulations in question. Contrary to petitioner's implication (see Pet. 16-17), cases from other circuits are no different. There, the arbitrators' decisions were based upon the collective bargaining agreements, while the courts' decisions were based upon statutes, regulations, and precedents that the arbitrators were not asked to (and lacked the authority to) interpret. *See, e.g.*, *International Brotherhood of Electrical Workers, Local 97 v. Niagara Mohawk Power Corp.*, 143 F.3d 704, 710 (2d Cir. 1998) (issue before arbitrators was "whether the just cause standard specified in Article XXII of the collective bargaining agreement was met") and at 719 n.13 ("The Panel was not asked to discuss, let alone resolve, the public policy implications of reinstating [the employee]").

This Court has emphasized the importance of this distinction by making clear that the scope of the parties' agreement to arbitrate is dispositive of such issues:

> [A] party who has not agreed to arbitrate will normally have a right to a court's decision about the merits of its dispute. . . . But, where the party has agreed to arbitrate, he or she, in effect, has relinquished much of that right's practical value. The party still can ask a court to review the arbitrator's decision, but the court will set that decision aside only in very unusual circumstances.

First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 942 (1995). The reason why courts "do not sit to hear claims of factual or legal error by an arbitrator" is "[b]ecause the parties have contracted to have disputes settled by an arbitrator chosen by them rather than by a judge . . . ." *Misco*, 484 U.S. at 37-38. As *Mitsubishi* made clear, these principles apply to the arbitration of disputes involving statutory as well as contractual issues. "By agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum." *Equal Employment Opportunity Commission v. Waffle House, Inc.*, 534 U.S. 279, 295 n.10 (2002) (quotation omitted). Petitioner presented its antitrust affirmative defense in arbitration, and it is bound by the arbitrators' decision. It is not entitled to relitigate this issue in court by recasting it as a public policy question.

4. Finally, this case would in all events be an especially poor vehicle to address the legal issue set forth in the petition. First, this case is not an instance where the court of appeals reversed a district court's ruling that petitioner's antitrust affirmative defense had merit. To the contrary, the court of

appeals recognized that the prohibition of a licensor competing against its own sublicensee only during the term of the licensing agreement "was a lawful ancillary agreement designed to induce Maruishi and its sublicensees to make the investments needed to bring the new drug to market." Pet. App. 6a-7a. There is little reason to believe that, were this Court to accept petitioner's invitation to prolong this litigation, the end result would be any different given the fact-driven nature of petitioner's affirmative defense — heard and rejected by the arbitral panel.[7]

Second, as described by the court below, petitioner, "as a producer, is a poor champion of consumers." Pet. App. 6a. Petitioner for years enjoyed the benefits of the agreement that it negotiated, which has and continues to entitle it to royalties based on respondent's sales. But now that petitioner has concluded that it can make higher profits by competing against its own sublicensee (which expended $1.434 billion to commercialize the product in the first place), it seeks to avoid its prior agreement. Pet. App. 3a. Moreover, as the court of appeals noted, having created any arguable antitrust issue by acquiring Ohmeda, petitioner "can solve unilaterally any antitrust problem" by divesting itself of Ohmeda and cannot use this self-created issue to attempt to deprive respondent of the benefits of its agreement. Pet. App. 7a. Similarly, in *W.R. Grace*, this Court rejected the employer's public policy defense because the purported violation of law "was of the Company's own making" (461 U.S. at 767) and because there was no justification to shift the burden of loss from the employer

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7. As the district court concluded (Pet. App. 39a-40a), petitioner's "FTC consent decree" affirmative defense likewise is meritless, because Baxter (as a non-party) lacks standing to enforce this decree (*Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 750 (1975)), and because this licensing arrangement is simply not contrary to the language of the decree in any event.

to certain of its employees, "who shared no responsibility for" the asserted illegality (*id.* at 770). Finally, as the court of appeals pointed out, others with more genuine concern for the public welfare can seek redress for the supposed antitrust issue raised by petitioner. Pet. App. 6a.

CONCLUSION

The petition for a writ of certiorari should be denied.

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No. 03-59

IN THE

Supreme Court of the United States

BAXTER INTERNATIONAL, INCORPORATED,
Petitioner,

v.

ABBOTT LABORATORIES,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

PETITIONER'S REPLY BRIEF

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PETITIONER'S REPLY BRIEF

Abbott's Brief in Opposition badly obscures the nature of this case. Abbott would have this Court believe this is an antitrust case. Br. in Opp. 1 (arguing Baxter contended that its defense "arose under federal antitrust law"), 8 ("antitrust affirmative defense"), 9 (same), 11 ("issue of federal antitrust law"), 12 ("a federal antitrust issue"), 14 ("antitrust affirmative defense"). It is not. This Court has made clear that a party raising a public policy defense to enforcement of an arbitral award must point to some "positive law" violated by the award. *Eastern Associated Coal Corp.* v. *United Mine Workers of Am., Dist. 17*, 531 U.S. 57, 63 (2000). Baxter pointed to the two sources of positive law implicated by the arbitrators' ruling: the antitrust laws and the FTC/Abbott Consent Decree. Had the arbitrators interpreted the contract to require Baxter to rob a bank, Baxter would have pointed to state and federal criminal law. From the point of view of the

public policy defense, the particular positive law the award compels a party to violate is a detail.

The central thrust of Abbott's Brief in Opposition is, thus, a distraction. Baxter did not attempt to relitigate in court an "antitrust claim" presented to and ruled upon by the arbitrators. And Baxter never "recast[]" an antitrust claim as a public policy question. See Br. in Opp. 14. Baxter has consistently presented its argument as one seeking to protect public policy, which happens to be embodied in the antitrust laws and in a consent decree.

The true nature of this case is quite simply stated: This is a contract case that was submitted to arbitration. Therefore, the following rules apply. In a contract case, a party is permitted to argue that its opponent's interpretation of the contract should be rejected because it would render the contract unlawful and hence contrary to public policy. *West Bend Mut. Ins.* v. *Mulligan Masonry Co.*, 786 N.E.2d 1078, 1088 (Ill. App. Ct. 2003).[1] Baxter thus urged the arbitrators to reject Abbott's proposed interpretation of the Sevoflurane and Dispute Resolution Agreements because Abbott's reading would render the contracts unlawful and hence contrary to public policy. After the arbitrators ruled, the question before the federal courts was whether to enforce the award. In an arbitration case, a party is permitted to argue against judicial enforcement of an award if it compels the parties to violate the law and hence public policy. *United Paperworkers Int'l Union* v. *Misco, Inc.*, 484 U.S. 29, 43 (1987); *W.R. Grace & Co.* v. *Local Union 759*, 461 U.S. 757, 766 (1983). Baxter thus urged the district court, and the court of appeals, to refuse to enforce the arbitration award because, by adopting Abbott's interpretation of the contract, the arbitrators compelled Baxter (and Abbott) to violate the law and hence public policy.

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[1] Illinois law controlled the interpretation of the contract.

The district court recognized its obligation to review the award to ensure that it did not compel a violation of public policy. The Seventh Circuit, over a dissent from one member of the panel and three members of the full court asked to rehear the case *en banc*, has held that when an arbitrator rejects a public policy contract defense, a court may not consider a public policy defense to enforcement of the arbitral award. As detailed below and in Baxter's Petition, the conflict between the Seventh Circuit's ruling and those of other courts is real and creates confusion in an area of the law—federal court review of arbitral awards—that demands national uniformity. This Court should grant the petition.

1. The Decision Below Cannot Be Squared With The Decisions Of This Court And Other Courts Of Appeals. Abbott's attempt to square the Seventh Circuit's holding with the decisions of this Court and of other federal courts of appeals fails for a simple reason: Abbott never acknowledges the Seventh Circuit's actual holding. Abbott argues this case involves a straightforward application of *Mitsubishi Motors Corp.* v. *Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985) (holding that antitrust claims that are arbitrated receive the same level of court review as any other claim) because it erroneously believes this case involves an "antitrust claim." Br. in Opp. 12 (arguing that "the *Mitsubishi* Court anticipated the circumstances presented here"). Once it becomes clear that the public policy holding of the Seventh Circuit has nothing to do with the fact that this case involves antitrust law (or a consent decree), the whole argument crumbles.

In fact, to the extent the *Mitsubishi* Court anticipated the circumstances here, it concluded that federal court review of the public policy question is always preserved. In *Mitsubishi*, this Court considered the possibility that a foreign arbitral panel might read certain provisions of a contract as a prospective waiver of the right to pursue antitrust remedies. 473 U.S. at 637 n.19. Such a prospective waiver had long been considered an unenforceable violation of public policy.

Id. (citing cases). This Court made clear that if the arbitral panel interpreted the contracts to include such an unlawful prospective waiver, a federal court would not enforce that award. *Id.*

This Court nowhere suggested that a federal court's hands would be tied if, as might be expected, the antitrust claimant first urged the arbitral panel not to read the contract to waive its right to seek antitrust relief precisely because such a reading would violate public policy. Indeed, this Court had already said that whether an arbitrator is first presented with and rules upon a public policy challenge is irrelevant because, "in any event, the question of public policy is ultimately one for resolution by the courts." *Grace*, 461 U.S. at 766. Later this Court made clear that parties concerned that an interpretation of a contract would violate public policy must argue the point to the arbitrator first, precisely because court review of an award for compliance with public policy always remains available. *Vimar Seguros Y Reaseguros, S.A.* v. *M/V Sky Reefer*, 515 U.S. 528, 540-41 (1995). When this Court in *Vimar* said that it would not have ordered the issue to be presented to the arbitrator unless it was certain that a federal court could subsequently review the award for compliance with public policy, *id.*, it left no doubt that public policy remains ultimately for the courts, no matter how the arbitrators treat the issue.

Abbott tries to distinguish this Court's statements in *Mitsubishi* and *Vimar* by arguing that a prospective waiver of statutory remedies is a "distinct circumstance" that justifies federal judicial review of an arbitral award. Br. in Opp. 12-13. But Abbott never explains why. There is no prospective-waiver-of-statutory-remedies defense to enforcement of an arbitral award. Rather, as this Court made clear, the prospective waiver of statutory remedies was important in *Mitsubishi* precisely because such a waiver is a violation of public policy, triggering the public policy defense to enforcement of an award. There is no basis in *Mitsubishi* or

any other case for treating one particular violation of public policy differently than any other violation of public policy. That is, if a court may review an arbitral award to ensure it does not order a prospective waiver of statutory remedies (as Abbott concedes), it also must review an arbitral award to ensure that it does not order a violation of the antitrust laws. The decision below cannot be squared with this Court's decisions outlining the proper role for the courts when presented with public policy challenges to arbitral awards.

Not only is the Seventh Circuit's decision impossible to square with this Court's words, it cannot be squared with the actions of other courts of appeals. Abbott denies that other courts of appeals have reviewed arbitral awards for compliance with public policy even after an arbitrator had been presented with and ruled upon the identical legal issues that make up the public policy defense. Abbott asserts that in the cases cited by Baxter, "the arbitrators were not authorized to, and did not, decide the issues later presented to the courts."[2] Br. in Opp. 13. This assertion is wrong.

In fact, the arbitrators and the courts in the cases cited by Baxter were presented with arguments that mirror Baxter's presentation to the arbitrators and the courts in this case. In all the cases, including this one, the arbitrators were asked to interpret the parties' contract. The labor arbitration cases involved an interpretation of the phrase "just cause," and this case involved an interpretation of the phrase "impairment of the original commercial relationship." In all the cases, including this one, the arbitrators were asked to reject one party's interpretation of the contract in light of certain positive law. The labor arbitration cases involved federal

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[2] Abbott cites no authority for the proposition that an arbitrator lacks the authority to consider whether a proposed interpretation of a contract should be rejected because it would violate public policy. There is none. Arbitrators are free to consider any legal issues presented in support of or against a party's interpretation of a contract.

safety regulations, and this case involved the antitrust laws and the consent decree. *International Bhd. of Elec. Workers, Local 97* v. *Niagara Mohawk Power Corp.*, 143 F.3d 704, 709 (2d Cir. 1998) (stating that the arbitrator "examined at length the Company's [interpretation] within the context of ... NRC regulations"); *Southern Cal. Gas Co.* v. *Utility Workers Union of Am., Local 132*, 265 F.3d 787, 792 (9th Cir. 2001) (stating that the arbitrator "concluded that the Gas Company failed to comply with the strict requirements of the federal regulations regarding DOT drug testing"); *Delta Air Lines, Inc.* v. *Airline Pilots Ass'n*, 686 F. Supp. 1573, 1575 (N.D. Ga. 1987) (stating that arbitrator considered the pilot's compliance with FAA regulations regarding consumption of alcohol by pilots), *aff'd*, 861 F.2d 665 (11th Cir. 1988). And in all the cases, including this one, the federal courts were later asked to review the arbitrators' awards for compliance with the same positive law that had been presented to the arbitrators. The Second, Ninth, and Eleventh Circuits all undertook their own independent reviews of the applicable (and previously presented) positive law to ensure the awards' compliance therewith. *Electrical Workers*, 143 F.3d at 715-19; *Southern Cal. Gas Co.*, 265 F.3d at 795-96; *Delta Air Lines, Inc.* v. *Air Line Pilots Ass'n, Int'l*, 861 F.2d 665, 672-74 (11th Cir. 1988). In stark contrast, the Seventh Circuit refused. There is no way to reconcile the approach of the other courts of appeals with that of the Seventh Circuit.

It is worth noting that none of the other courts considered it significant that the substantive legal issues that form the public policy challenge had been considered by the arbitrators at the employers' invitation. Abbott, on the other hand, appears to attach some significance to the fact that Baxter presented the antitrust and consent decree issues to the arbitrators, at least if repetition is any indication of significance. Br. in Opp. 1 (noting Baxter "submitted" the issues to the arbitrator), 8 ("petitioner expressly invited the tribunal" to consider the issues), 9 (arbitrators considered

issues at "petitioner's own express invitation"), 10 (arbitrators considered issue at "petitioner's own invitation"), 11 (same). This numbing repetition does not, however, reveal what relevance the point has to this case.

Perhaps Abbott believes it best for parties to withhold from the arbitrators a public policy rationale for rejecting a proposed contractual interpretation so that the public policy argument can be presented exclusively to a court. Abbott does not, however, explain why courts should adopt a rule that discourages parties from presenting all their arguments to the arbitrators. Indeed, the Fourth and Seventh Circuits have rejected that approach. Those courts have held that the failure to argue an issue before an arbitrator waives judicial review of the award on the ground not presented. *District 17, United Mine Workers of Am.* v. *Island Creek Coal Co.*, 179 F.3d 133, 140 (4th Cir. 1999); *Baltimore & Ohio Chi. Terminal R.R.* v. *Wisconsin Cent. Ltd.*, 154 F.3d 404, 409-12 (7th Cir. 1998). A full airing of the issues before the arbitrator makes sense, even if the courts ultimately will be required to rule on the issue. Hiding legal issues from arbitrators which bear on the questions before them can only hamper their ability to produce proper rulings. Further, presenting the issue to the arbitrator allows the parties to put the relevant facts on the record, which will facilitate court review. Baxter thus properly presented the arbitrators with the public policy issues that it has also properly presented to the courts.

In the end, the Seventh Circuit's rule produces bizarre results. Assume a party's opponent in an arbitration asks the arbitrators to interpret the contract to compel the parties to violate the law (criminal law, the tax code, antitrust law, or any other positive law). Assume further that the party informs the arbitrators that if they adopt the proposed interpretation, a court will not enforce the award because the award would violate the public policy expressed in that law. And assume finally that the arbitrators expressly reject that view. According to the Seventh Circuit, precisely because the

arbitrators were warned of the possibility that a court would refuse to enforce their award and they adopted the controversial interpretation anyway, the court cannot refuse to enforce the award. This makes no sense and threatens to undermine the critical role this Court has reserved for federal courts to police arbitral awards that violate the public policies reflected in positive law.

2. The Seventh Circuit Has Not Decided The Antitrust Issue. Abbott lastly argues that this Court should decline to review this case because the Seventh Circuit decided that the arbitration ruling did not create an antitrust violation. Br. in Opp. at 8, 14-16. This is demonstrably false. While Judge Easterbrook's opinion offers passing remarks on the question, his opinion is explicit that those remarks did not reflect his (or the Court's) considered views. The panel majority underscored that it considered the merits of the public policy defense only casually by refusing to consider at all whether the award's conflict with the consent decree warranted setting it aside. Pet. App. 7a. The opinion is crystal clear: the substantive public policy claims are "unnecessary to pursue" because "[a]ll that matters today is that the arbitrators have concluded that the antitrust laws" were not violated by their award. *Id.*

Only one appellate judge offered his considered views on the question, and he concluded that the award, in fact, does violate the antitrust laws. Contrary to the passing, single-paragraph musings offered by the panel majority on the antitrust question, Judge Cudahy's dissent carefully analyzes the facts of record against the governing legal standards and concludes that the covenant not to compete imposed by the arbitrators could not have been ancillary to the agreements to produce sevoflurane and could not have had any procompetitive effect. Pet. App. 14a-17a. The antitrust issue presents serious questions that, for the reasons discussed above, a court must confront *de novo* and should not abdicate to arbitrators.

Finally, three of the eight judges of the full Seventh Circuit to review the petition for rehearing *en banc* considered the public policy ruling of the panel sufficiently serious on its own to merit further review. As these judges recognized, the holding of the panel "clouds the authority of [a federal] court to review arbitration agreements of private parties that violate public policy—an authority repeatedly acknowledged by the Supreme Court." Pet. App. 94a. The risk that the decision below will hamper the ability of federal courts to review arbitral awards for compliance with public policy is, by itself, a compelling reason for this Court's review.

CONCLUSION

For the foregoing reasons, and those stated in Baxter's Petition, the petition should be granted.

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